S. HRG. 103–718

PREVENTING ABUSE OF FmHA'S LOAN PROGRAMS

Y 4. AG 8/3: S. HRG. 103-718

Preventing Abuse of FmHA's Loan Pro... ING

THE

SUBCOMMITTEE ON
AGRICULTURAL CREDIT
OF THE

COMMITTEE ON AGRICULTURE,
NUTRITION, AND FORESTRY
UNITED STATES SENATE

ONE HUNDRED THIRD CONGRESS

SECOND SESSION

ON

PREVENTING ABUSE OF FmHA'S LOAN PROGRAMS

FEBRUARY 3, 1994

Printed for the use of the
Committee on Agriculture, Nutrition, and Forestry

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PREVENTING ABUSE OF FmHA'S LOAN PROGRAMS

THURSDAY, FEBRUARY 3, 1994

U.S. SENATE,
SUBCOMMITTEE ON AGRICULTURAL CREDIT,
COMMITTEE ON AGRICULTURE, NUTRITION, AND FORESTRY,
Washington, DC.

The subcommittee met, pursuant to notice, at 10:10 a.m., room SR–332, Russell Senate Office Building, Hon. Kent Conrad, Chairman of the subcommittee, presiding.

Present or submitting a statement: Senators Conrad, Leahy, Lugar, Daschle, Kerrey, and Grassley.

STATEMENT OF HON. KENT CONRAD, A U.S. SENATOR FROM NORTH DAKOTA

Senator CONRAD. This hearing before the Subcommittee on Agricultural Credit of the Committee on Agriculture, Nutrition, and Forestry will come to order.

This hearing is on the subject of preventing abuse in FmHA loan programs. I first want to thank the Administrator, Mr. Dunn, for agreeing to appear at this hearing in a very short time frame. I want to commend Mr. Dunn for being prepared for a hearing on a subject of this complexity and this magnitude in such short order, and I very much appreciate the detailed documentation that you have provided to the committee.

I want to welcome everyone else who is here. I called this hearing because of the *Washington Post* story that appeared last Friday on abuse of FmHA's loan programs by borrowers with millions of dollars in assets. I must say I was angered by the examples of abuse in that story, and I want to publicly commend the *Washington Post*, and the writer of that story, for what I think, is a public service in bringing to light the names of some of the people, and specific examples of abuse.

First, I want to establish at this hearing why we are not collecting on these loans. Under the law, a borrower who is delinquent on his FmHA loan must be forced into foreclosure unless that borrower meets two clear conditions: number one, the borrower must be delinquent due to circumstances beyond his or her control; and, two, the borrower must have acted in good faith.

The plain interpretation is that a multi-millionaire who refuses to pay his or her loan is not delinquent due to circumstances beyond their control and is clearly not acting in good faith. Therefore, under the law, the FmHA should be foreclosing on millionaires and others who will not repay.

That is the basic outline of existing law.

The purpose of this hearing is to answer several questions which I think the public would like to see answered today:

One, has FmHA failed to collect delinquent loans from wealthy borrowers who have the assets to pay, or are the farmers mentioned in the *Washington Post* article rare exceptions to the rule?

Number two, what is FmHA's strategy to collect the remaining delinquent loans of wealthy individuals and others who are delinquent?

Three, is current law adequate or are changes needed to facilitate collection from wealthy individuals and others who clearly have the resources to pay?

I think it is also important to point out that the loans obtained by the individuals of the *Washington Post* article are no longer available. Congress has turned off that faucet. Congress eliminated one emergency loan program and sharply curtailed the other, which was responsible for most of these delinquencies. I might add that was long before I came to this body. Congress identified the problem and acted to either kill or curtail the programs that gave rise to these abusive situations. It also limited loan eligibility to family-sized farmers who personally provide the majority of the labor for their farming operations, and it sharply limited the amount any one farmer can borrow.

We have a new administration now at USDA and a new Administrator of Farmers Home. Mike Dunn has been in this job for just 2 months. So we want to again publicly commend him for being ready and willing to address this important issue on such short notice, and, again, I was very pleased with the level of documentation that you have provided the committee.

I am very pleased that my colleague, Senator Lugar, is here, the ranking Member of the Full Committee, somebody who has been pursuing these issues very vigorously the entire time that I have been in the Senate, and I am sure before that. I want to turn to him at this point for any statement that he might have.

Senator Lugar?

STATEMENT OF HON. RICHARD G. LUGAR, A U.S. SENATOR FROM INDIANA

Senator LUGAR. Thank you very much, Mr. Chairman. I commend you not only for calling this hearing and Mr. Dunn for appearing, as you pointed out, in a very short time frame, but your diligence on these issues throughout your career in the Senate.

I just simply want to comment briefly on the recent article in the *Washington Post*. I think the record, as you pointed out, Mr. Chairman, should reflect the fact that some of the issues on the loans that are spoken of did occur over 10 years ago. One important new item pertains to the impact of the moratorium imposed on March 5, 1993, by Secretary Espy, and the delay in resolving conclusively the long outstanding problem loans.

This FmHA situation has been the subject of much legislative activity by our committee over the years. Often I believe that we have not been fair to either the taxpayers who ultimately foot the bill or to the borrowers. Over the years we have put into the statute provisions that, while good intentioned, have insulated borrow-

ers on occasions from the realities of the financial marketplace. We have instituted generous borrower rights and appeals procedures that disadvantage sound management and loan collection. While these provisions have effectively delayed the inevitable, the interest costs associated with those loans have been mounting, in many cases to a point where any equity the borrower had was lost.

I have another concern as well. As Members of this committee know, my USDA restructuring proposals were not only efficiency oriented, but also defensive in nature. I firmly believe that our more urban-oriented colleagues will decide that USDA and the farm programs are badly in need of reform and will demand timely and thorough action. In that environment, the USDA budget could be dramatically reduced. I have long believed it is incumbent upon those of us involved in agriculture to get our house in order to defend our programs against those that criticize them.

Articles such as the one appearing in the *Washington Post* will certainly hasten the day when USDA and the programs under its jurisdiction will come under closer scrutiny of those not predisposed to support agriculture. In many situations, FmHA lending is necessary, in situations such as the beginning Farmer Program or in the short term to those truly unable to secure credit elsewhere. The Program has often been badly mismanaged, primarily because of directives from Congress. The Agency, by and large, is often hamstrung in its ability to act forcefully to clean up problem debts. The end result is that those debts grow larger and larger, in the billions each year.

We cannot continue to hold farmers harmless from the economic perils of farming. It is imperative that we change the direction of the Farmers Home Administration lending programs and allow the Agency management to make tough decisions to more prudently manage taxpayer resources.

The first issue that should be addressed pertains to the moratorium on foreclosures, imposed by Secretary Espy, on March 5, 1993. As I told the Secretary at the time in a letter, I was concerned about his action and that I was in disagreement about the necessity of such an action. As the current statute today stands, the farmer borrower already has the tables tilted strongly in his or her favor. Borrowers are given considerable deference in the package of borrowers rights that FmHA is obligated to offer. Should that offer not be entirely to the borrowers' liking, Congress in 1987 instituted an appeals procedure that further disadvantages management.

I do not quarrel with procedural safeguards, but if the end result is to freeze the actions of the Agency, we are doing a grave disservice to the taxpayers of the country and the Agency. The data supports that argument. Of the 10,109 borrowers that have received a writedown of their obligations to FmHA, some 2,064 borrowers, or over 20 percent, are already delinquent again in their payments.

The second issue necessary for action is to eliminate the ability of a borrower once that borrower has received a writedown or writeoff from receiving another loan. Current law requires FmHA to ignore past repayment history when considering a borrower's request for a new loan. That requirement ignores the reality that a borrower that does not feel obligated to repay previous debts

may not feel obligated to repay those incurred in the future. Other lenders place a high priority on the past repayment practices of borrowers. That is what credit histories are all about.

Mr. Chairman, I have outlined two items I believe are necessary to begin the transformation of the FmHA into a more prudent lender where repayment is expected and tough choices are made. If the Agency acts responsibly today, then it will, in my opinion, be around in later years to assist young and beginning farmers—the Agency's original mission. I believe in that mission. I am reminded of the powerful testimony given several years ago before this committee by Jim Mosely, a farmer from Indiana who served as an Assistant Secretary of Agriculture. Jim did not grow up on a farm, and he got his start in farming from the FmHA. Other lenders laughed at this young would-be farmer, but FmHA did not, and today he is probably one of our State's top producers. We must allow this Agency to return to this high calling.

I thank you, Mr. Chairman.

Senator CONRAD. Thank you, Senator Lugar.

Welcome to Mike Dunn, the Administrator of FmHA. Please proceed with your testimony. Unlike usual practice, I would ask you not to summarize. I would ask you to give your full testimony because I think it is very important that the full story be told here today in terms of what you intend to do to go after these delinquent loans, what specific steps are under way to assure the taxpayers of this country that those who have assets and owe the Federal Government money are, in fact, going to be required to repay. Number two, I think it is very important that we also lay out the record with respect to what has happened to the underlying programs that gave rise to this problem. Because as I indicated in my opening statement, the underlying programs have been either killed or sharply curtailed by the Congress in the past, but that still leaves us with the problem of collecting on these delinquencies.

Mr. Dunn, please proceed.

STATEMENT OF MICHAEL V. DUNN, ADMINISTRATOR, FARMERS HOME ADMINISTRATION; ACCOMPANIED BY BONNIE LUKEN, DEPUTY GENERAL COUNSEL, UNITED STATES DEPARTMENT OF AGRICULTURE

Mr. DUNN. Thank you, Mr. Chairman. Senator Lugar, thank you very much. I would like to introduce the person at the table here with me: Bonnie Luken, Deputy General Counsel for the Department of Agriculture. She has agreed to accompany me here today in case there are some specific legal questions that you would like to pursue.

I appreciate this opportunity to discuss this important issue of these large and complex loans and the delinquency rate at the Farmers Home Administration.

I want to say at the outset that the Clinton administration is outraged at the thought that wealthy individuals are not satisfying their just debts to the Government. This was exactly the type of situation that the President and Vice President set out to rectify as they sought to reinvent government. I pledge to you, as the President's representative, that we at Farmers Home Administra-

tion will do everything humanly and legally possible to collect every dime that is owed to the American people.

Million-dollar loans are no longer available from the Farmers Home Administration. You are right, Mr. Chairman. The loans reported by the *Washington Post* were made under emergency loan authority. Amendments to the Congressional Act in 1980 gradually reduced the maximum emergency loan to $500,000 for any one disaster. This legislation also phased out the bonus annual operating and major adjustment loans; that is, they could come at any time within the next 5-year period and get an adjustment loan. The Food Security Act of 1985 limited emergency loans to family-size farmers and prohibited loans to farmers eligible for credit elsewhere. Further, direct operating and ownership loans are now limited by law to $200,000; guaranteed operating loans are capped at $400,000; and guaranteed ownership loans cannot exceed $300,000. In all cases, the borrower must be a family-size farmer or rancher.

Before I discuss the large delinquent loans, I would like to take a minute to share with you the Clinton administration's philosophy on the mission of the Farmers Home Administration. Senator Lugar, I think this gets to the heart of what you addressed. Farmers Home is required to provide assistance to only those farmers who are unable to obtain credit from commercial sources. Typically, our borrowers are family-sized farmers. Many lack production resources, such as productive land and modern buildings and equipment. Many also lack the personal resources, such as sufficient education and experience, which provide the foundation for management skills critical for success. We view it as our mission to assist these farmers any way possible, not just to get credit, but to become credit-worthy, successful farmers.

That is why I firmly believe that we must provide supervised credit for these borrowers. This involves working closely with the borrowers from day one, to nurture, teach and counsel them. This is accomplished through frequent and thorough monitoring of the borrower's farm production and financial management, to pursue strategies that develop actions necessary to achieve the customer's planned objectives. Thus, farmers receive technical assistance, as well as individual counseling and evaluations necessary to focus corrective measures on the specific factors that might otherwise limit or prevent their success.

Unfortunately, in the past, Farmers Home has gotten away from providing supervised credit as the Agency's focus shifted to larger, wealthier farmers. Those days are now over. Our State directors are aware that supervised credit is one of the Clinton administration's top priorities, and efforts are already under way to provide training to employees to accomplish this goal.

During the Clinton administration's tenure, Farmers Home's focus will be to provide skillful assistance to small, limited resource farmers. Unfortunately, there remains at this time the unresolved backlog of large delinquent loans left over from the past decade, when large wealthy farmers were granted emergency loans. These are the subject of the *Post* article.

This article serves a useful purpose, as you point out, Mr. Chairman. It sheds light on the past policy decisions which have resulted in problems that have been festering in the Agency for years. These

problems, which we have already discovered, demand prompt and decisive action.

My colleagues at Farmers Home have been aware, and concerned about the enormity of the outstanding debt which has accumulated from delinquent large loans made years ago. Resolution of this situation was one of the first issues that I pursued, upon taking my oath of office, in November.

Today's hearing provides an opportunity to bring you up to date on our recent activities with respect to these large delinquent loans, as well as the related foreclosure suspensions. In addition, we will cover steps which we are taking to return Farmers Home to its traditional mission of providing supervised credit to small and limited-resource family farmers and ranchers.

I cannot emphasize too strongly the Clinton administration's conviction that Farmers Home's mission is to assist the small, limited resource family farmer, and it is paramount that we do so. This is the central mission that President Clinton, Secretary Espy and I, as the Administrator, intend to see Farmers fulfill.

First, the foreclosures: I would like to comment on Secretary Espy's suspension of foreclosures, which has been in effect since March 5, 1993. Allow me to provide a brief summary of the effect of the suspension on the resolution of the large delinquent loans.

As of March 5, there were 4,833 cases in the foreclosure process. Of this number, the Department of Justice had 962. Of the 4,833 cases, 240 were borrowers who owed more than $1 million. In March and April of 1993, Secretary Espy mailed out 3,913 letters to borrowers in foreclosure, providing them with the opportunity to request a review at the Secretary's level, to determine if their loans had been properly serviced, before being submitted for foreclosure.

Of the 3,913 farmers who received letters, 1,090 responded with a request for review. Of that 1,090 who requested a review, 100 borrowers were borrowers who owed Farmers Home over $1 million. Of the 100 borrowers who were reviewed, 23 of these loan dockets were sent back to the States for corrections in the servicing procedure. In other words, we found errors in what had taken place.

In California, six large loan borrowers requested a review by the Secretary's office. The review showed that all had been properly serviced, and the State was instructed to continue with foreclosure. None of the borrowers in the *Washington Post* article requested a review.

In summary, of the 100 large loan borrowers who requested a review, 66 were sent back to proceed with foreclosure. I am announcing here today that Secretary Espy has indicated that he is in the process of his own personal final review of Farmers Home's findings and anticipates the announcing of the lifting of this suspension by next week.

Overall, this suspension served as a very important purpose. In addition to guaranteeing the rights of those whose documents were reviewed, the suspension identified weaknesses in the foreclosure procedures that we can now correct.

A checklist of items has been developed for use in the field when the suspension is listed. It is Attachment 1[1] in the package that we have provided. The checklist addresses loan servicing weaknesses discovered by the review. This checklist will be used by district and State office personnel to ensure that all required notices have been provided to the borrower. It will also document that all required servicing actions have been completed prior to acceleration and/or foreclosure of all direct farm program accounts. Accounts previously reviewed by the Office of the Secretary and returned for litigation will not be subjected to this review.

The large loans referred to in the *Post* are indeed a problem to Farmers Home Administration. They will be a significant drain on the U.S. Treasury. It is apparent that some of the loan funds in question may never be recovered.

There are currently 971 delinquent large loans—that is loans of more than $1 million. The total principal and interest outstanding on these large loans is $2.2 billion, which is Attachment 2[2] of our provided material. The average loan side is $2.3 million. 110 of these loans, valued at $562 million, are located in California.

The large delinquent loans should be considered in the context of the entire Farmers Home portfolio. Currently, there are 136,050 Farmers Home borrowers, of which 1,030 (less than 1 percent) were million-dollar borrowers. This is Attachment 3[3] or Chart no. 1 that we have provided here.

You can see the total pie—.75 percent are those that are $1 million or more borrowers from Farmers Home Administration. However, these million-dollar borrowers comprise almost 40 percent of the total delinquent principal and interest, which is this pie chart here, which is also attached to our handout material. So less than 1 percent equals almost 40 percent of the total delinquency. In addition, these borrowers represent only 3.5 percent of the total delinquent borrowers.

The typical Farmer Program loan stands in stark contrast to this portfolio of large delinquent loans. In 1993, the average farm loan was $75,106, and was provided to a farmer with assets of $313,000. The average family living expenses for the farmer receiving direct farm program loans was only $17,000 per year.

On the other hand, over a decade earlier, million-dollar loans were made to large corporate entities and partnerships, which, among other things, refinanced existing debt from commercial lenders. The principals in these entities were often wealthy individuals with numerous non-farm business interests, such as real estate development. The loans were not underwritten by cash flows, rather, by assumed property values or, even worse, projected increases in property values. When property values collapsed, the security of the loans collapsed, as well.

When many large loans were made, several parts of the country, including California, had experienced a series of natural disasters. First, there was a severe drought in 1976 and 1977 affecting States in several regions. When the rains finally came in California, there was extensive flooding. Farms were deluged. Shortly thereafter,

[1] See Appendix, page 35.
[2] See Appendix, page 39.
[3] See Appendix, page 40.

flooded farmers in California, and drought-stricken farmers from the South and other areas, turned to Farmers Home for help. Thus, the large emergency loans were made. This is the genesis of the loans for the emergency assistance.

The economic situation at this time: Following this series of natural disasters, U.S. farmers were plagued by severe economic problems. The value of farm land dropped precipitously, and commodity prices collapsed.

The total value of farm assets decreased from just under $1.1 trillion in 1981, to about $850 billion in 1986. This is demonstrated in Chart 3. Total farm equity decreased from $910 billion in 1981, to $681 billion in 1986—a 25 percent decrease. Interest rates averaged 12.87 percent for most of the period, and peaked in 1981 at 18.87 percent. At the same time, the value of agricultural exports decreased from $43.3 billion in 1981 to $26.2 billion in 1986, a 40 percent drop. These factors combined to create a crisis in the agricultural sector which caused all lenders to experience severe losses on their agricultural portfolios.

Remember, Senators, I had pointed out that this agricultural asset is what these emergency loans were based upon.

Between 1985 and 1986, the Farm Credit System, commercial banks and life insurance companies all took huge losses. Losses to commercial banks peaked in 1985 at $1.3 billion; losses to the Farm Credit System peaked in 1986 at $1.3 billion; and life insurance losses peaked in 1986 at $827 million. Farmers Home Administration losses, however, did not peak until 1989, when Farmers Home lost $3.3 billion.

From 1981 to 1989, 311 agricultural banks failed. In fact, the situation became so critical that, in 1987, Congress enacted legislation to provide financial assistance to the Farm Credit System to prevent it from collapsing. Due to policy directions and statutory and legal mandates, Farmers Home did not work out problem farm loans in the mid–1980's, as had been done by other financial institutions. As a consequence, Farmers Home losses occurred later in the 1980's, when compared to other lenders.

When it became apparent to commercial lenders and the Farm Credit System in 1985 and 1986 that many loans could not be repaid, because farmers were in desperate economic straits, many loans were written off. At the same time, some lenders concerned about mounting loan defaults discontinued making agricultural loans. Many of the borrowers who were refused credit by the commercial lenders wound up at Farmers Home Administration.

In the private sector, once it is determined that commercial loans cannot not be repaid, interest stops accruing and the loan is quickly written off. Unlike these financial institutions, Farmers Home continues to accrue interest on bad loans. Thus, even when it is determined that a farmer is incapable of making payments, interest continues to accrue.

This, in part, explains the continued increase in farm loan losses, which turned up sharply after 1986. Farmers Home charge-offs include both principal and interest, while private lenders only charge off principal. Of Farmers Home's $14.8 billion in charge-offs since 1984, approximately 30 percent represents interest. In other words,

excluding interest, the principal charged off would be approximately $10 billion.

One of the main impediments to Farmers Home writing down loans resulted from two lawsuits, *Coleman v. Block* and *Curry v. Block*. The decision in the *Curry* case was that Farmers Home had failed to publish regulations affording borrowers relief provided for by Congress. The judge in *Coleman* ruled that Farmers Home regulations adopted in response to *Curry* did not provide sufficient information on borrowers' options. In 1983, Farmers Home became the subject of a nationwide injunction against foreclosures.

For most of 5 years following the commencement of the lawsuit, until February 1989, Farmers Home was unable to accelerate most of the loan accounts, because the Agency was prohibited from initiating foreclosure actions during this time. Any delinquent loans went unserviced, and interest continued to accrue.

I think this is a crucial point, Senators, because it shows what happened in 1985 and 1986, as the commercial institutions realized that there were problems, and this is the height. This is when you met and did the 1987 Credit Act. They stopped accruing interest. They put those loans in non-accrual accounts, they wrote them down or, better yet, they got them written down to where they became accruing loans, working loans again, and were able to again accumulate interest for those private institutions.

We in Farmers Home Administration were not allowed to do that, because of the situations that I have just outlined. You see, our losses continued to rise, until we finally got laws in place and regulations in place, and now they are beginning to drop.

Congress addressed these problems by enacting the Agricultural Credit Act of 1987. The Act prescribed in detail loan servicing options to be afforded delinquent farm borrowers. Although enacted early in 1988 to authorize restructuring of debt, it was not until 1989 that the Act was actually implemented. The main features of the Act provided for write-downs of loans to the current value of collateral, if the cost was equal to or less than the return from liquidation; buy-outs for the net recovery value of Farmers Home of the collateral securing the loan; stronger homestead protection and farm buyback provisions; and establishment of an appeals division separate from the Agency's loan operations.

All of these are sound financial decisions. It told the Agency, if you could reap more money for Treasury by writing down the loans and getting them working again, do so. If not, take a buyback at the net recovery cost of those loans.

It should be noted that the appeals process provided much-needed objectivity to ensure borrowers' rights. However, it has inadvertently provided opportunities to significantly delay the foreclosure process. For instance, if a borrower exercises all of his or her servicing and appeal rights, the process could continue for 1,200 days. This amounts to 3 years plus 105 days, the maximum statutory time frame prior to foreclosure. This serves to explain why some large delinquent loans will still take some time to be resolved.

During this same time period, there were significant staffing decisions which contributed greatly to the current situation.

There is no question in my mind that the Farmers Home field staff worked as hard and as creatively as they could to handle the tidal wave of new loans in the early 1980's. Their resources and training, however, fell short of the demands placed upon them.

During this period, there were staffing increases at the national headquarters and in the Agency's finance office in St. Louis. The total number of Farmers Home employees in these two offices had grown to more than 1,700, of which only 250 were loan specialists.

This is why Secretary Espy has developed a reorganization plan for the United States Department of Agriculture. It is his intention to redirect the human and fiscal resources of the department, to provide services needed to accomplish the department's mission.

Mr. Chairman, although we are well aware that this large loan situation cannot be repeated, every effort must be made to clean up the mess created in the last decade. We at Farmers Home have already begun this process, by implementing the following procedures:

In 1992, a Large Loan Servicing Group was created in response to the difficulties experienced in attempting to resolve these large delinquent accounts. This group is comprised of professionals from nationally prominent law firms and financial institutions specializing in managing problem loan portfolios. The number of delinquent loans over $1 million, as a result, has fallen from 1,400 to 971 since the inception of this group.

The Large Loan Servicing Group has identified areas of concern and has focused their efforts on changing ineffective processes to resolve these accounts. It has also forced the borrowers to address their obligations to Farmers Home Administration. In 1993, this group conducted a 4-day training session with Farmers Home representatives from every State. From these States were selected problem loan coordinators, who discussed problem loan resolution strategies and action plans, litigation and bankruptcies, and ways to identify hidden assets.

Farmers Home instituted a procedure to contract with private asset investigation firms to identify assets that were not reported to Farmers Home by these borrowers. This effort has already uncovered significant instances of fraud and conversion.

All States have action plans in place to resolve delinquent accounts, which are reviewed by the Large Loan Servicing Group. This group is also traveling to the State offices to conduct extensive portfolio reviews, to help establish specific action plans for resolving these accounts.

Farmers Home has recently developed improved coordination efforts with the USDA Office of the Inspector General, to obtain assistance with investigations of large delinquent borrowers who display signs of fraudulent or other criminal action.

USDA is currently working to implement a litigation tracking system, which will assist in identifying those cases which are not receiving the attention necessary to permit timely litigation.

The Secretary has directed me to develop legislative proposals to deal with this situation. These proposals will likely include a request for additional statutory changes to permit the hiring of private counsel to go after these cases, and we will be using USDA field attorneys, making them special agents of U.S. Attorneys.

Efforts have already been undertaken by the Large Loan Servicing Group to move additional authorities to State Farmers Home offices to resolve those cases without assets or legal merit. This permits the Large Loan Group to focus on those cases with significant assets remaining.

You have in your packet a matrix in which we look at these loans, and we have divided them into those that have collateral available that we can go after and those that we do not have collateral available. Those that have extended or past the 6-year statutory review period and those that have not, and we have identified those that have assets, that the statute of limitations have not run out on, and those are the ones that the Large Loan Group is going after to collect every dime that we can.

It is clear we need to get beyond these large delinquent loans. Mistakes were made. Congress has taken steps to close loopholes, so that this situation will never reoccur. Now we must cut the losses resulting from past poor policy decisions. Gentlemen, there will be large writeoffs. The loans are still on the books. Farmers Home must take the same hit that private individuals and commercial lenders took in the 1980's.

We must now proceed with our real mission—providing credit to small, limited resource farmers who cannot secure credit elsewhere. This can only be done through supervised credit. Supervised credit will allow Farmers Home to prevent defaults, by building quality up front. Merely providing loans does not help farmers in the long run, if they do not have a management plan, if they do not have a bookkeeping system, if they do not know how to keep current and accurate records.

Supervised credit means identifying strengths, as well as weaknesses, and then developing a plan to capitalize on the strengths and correct the weaknesses. Our objective is straightforward, to increase the potential for the borrower's success and graduation to other credit, while minimizing the cost to the Government. There is no other banking institution which provides this type of personal service to this segment of the farming community.

In order to gauge our success at Farmers Home Administration, I hope you will focus on our ability to meet our supervised credit priorities in the future. We will clean up the large delinquent loans. On that, you have my word. We currently have 971 large delinquent loans. Within 12 to 24 months, I hope to report to you that all of those that are not tied up in the servicing, appeals or litigation process have been settled. Our first priority will be to address the 683 cases where there is still collateral. We will make every effort to recover as much as possible on behalf of the Federal Government.

In the future, I hope you focus on how well we achieve our commitment to small farmers. Judge this administration by the number of small farmers we have served, by the number of beginning farmers that have gotten an opportunity to own farms of their own, by the number of socially-disadvantaged farmers that have been given an opportunity to stay on the farm, and by the number of family farmers that have averted financial ruin because of supervised credit.

Mr. Chairman, and Members of the subcommittee, I thank you for the time you have given me, and I look forward to answering any questions that you might have.

Senator CONRAD. Thank you very much for that testimony.

The Chairman of the full committee has arrived, and I would turn too him for any statement that he might want to make.

STATEMENT OF HON. PATRICK G. LEAHY, A U.S. SENATOR FROM VERMONT

The CHAIRMAN. Thank you, Mr. Chairman.

I will be brief and I will put my whole statement in the record.

I am glad to have Mike Dunn here. I read his statement before coming in, and I appreciate having it read again. I think it is an important one and lays out the history well.

You and the Secretary inherited a major crisis with these thousands of large, delinquent and improperly serviced Farmers Home Administration loans. A lot of them were made more than a decade ago. They were made to rich farmers with sidelines like developing golf courses or luxury housing. Instead of buying tractors, they were buying airplanes.

I think that these large businesses bear no resemblance to the small limited resource farmers that the Farmers Home Administration was set up to help, and I know that they bear no relationship to the kind of small farmer that you and the Secretary are intent on assisting. They are really sophisticated scofflaws who deserve to be taken to task, and I think they ought to be taken to task in the name of all the small farmers and small businesses that really work at following the rules and paying the bills.

These multi-million-dollar loans were not written based on what was projected as cash flow. They were based on what was projected as possible increases in land values. Even without good cash flow, a lot of the borrowers are so well-heeled. They can hire all the lawyers they want to throw sand in the wheels of collections.

In fact, they took shelter under the 1983 court injunction that was stopped all foreclosure actions nationwide for 5 years because of the improper handling of loan servicing by Farmers Home. I stress again, mismanagement before you or Secretary Espy were there. We took action in 1987 that resulted in the end of the injunction, and then further tightened and improved the farm loan program in the 1990 farm bill. I think it is good that you are going to get to the bottom of this, and I think the time is now, and I do not think you have much time left. I think you have to be very, very aggressive on it.

I am glad to hear the possibility that the moratorium will be lifted. We ought to figure out a better way to do business, to ferret out the assets of wealthy deadbeat farmers, and to collect every penny than can be collected talking about wealthy deadbeats. If it was somebody who was barely making it, we would be down there saying you have got to pay this back, you have got to pay this back.

We have people flying back and forth in their private planes or going on yachts or going to their beach houses. These are not the kinds of farmers that I see in Vermont or we see in Indiana or North Dakota or Nebraska. I mean these are not farmers. These are people who are enjoying the luxury of a hobby and letting the

American taxpayers pay for it. I think that is wrong. We should not have part-time farmers living in $800,000 condominiums or developing golf courses or running big non-farm businesses, when they owe the Farmers Home Administration millions of dollars. This is not the free enterprise system. It is free to them. The enterprise is on the part of the American taxpayers to have to pay for it, and they just figure they can keep it going with a lot of time-consuming appeals, which I think is also wrong. This is not the way it was set up.

You know, I think a lot of hard-pressed farmers in Vermont, many of whom wait in long lines to get limited Farmers Home credit, are pretty sick and tired of the abuses too. These are the people who we set up the Farmers Home Administration to assist, and somehow they got forgotten.

The farmers that are looking for help live along rocky hillsides. They are not in an ocean-side villa. They drive tractors. When they talk about some antique that they have, they are not talking about a vintage airplane that they have in their collection. They are talking about an old Ford tractor that has to keep eking out 1 more year. The transmission will be taken apart and put back together one more time, because they cannot buy a new one. They do not have lawyers on retainer, and they milk Holstein and Jersey cows—not Federal farm credit programs.

Mike, I am glad you are here, I must say. I also want to congratulate Kent Conrad for holding this hearing, on very short notice. Frankly, Mr. Chairman, if legislation is recommended that they need for this, I can assure you we will meet very quickly in the full committee on it. I think this is something we will find Republicans, and Democrats alike, will join in on. Nobody wants a program used this way.

I will put my whole statement in the record. Thank you for having this hearing.

[The testimony resumes on page 15.]

[The prepared statements of Senator Leahy and Senator Daschle follow in subsequent order:]

STATEMENT OF SENATOR PATRICK J. LEAHY

Secretary Espy inherited several major challenges in January of 1993. Two days before President Clinton's inauguration, children became seriously ill in a food poisoning disaster in Washington State.

The Secretary had to devote his time and energies to managing that crisis, which he did very effectively.

The Secretary also inherited another crisis—thousands of large, delinquent, improperly serviced Farmers Home Administration farm loans. Loans unwisely made more than a decade ago to rich farmers with sidelines like developing golf courses and luxury housing and buying expensive classic airplanes.

In fact, these big businessmen bear no resemblance to the small, limited resource farmers that I know Secretary Espy and FmHA Administrator Dunn are dedicated to assisting. They are sophisticated scofflaws who deserve to be taken to task in the name of those small, family farm borrowers who play fair and pay regularly.

The multi-million dollar loans in question were underwritten not on the basis of healthy farm cash flow, as they should have been, but on projected increases in property values. Even without good cash flow the well-heeled borrowers could still afford to retain expensive lawyers to block collection efforts.

These high rolling delinquents took shelter under a 1983 court injunction that stopped all foreclosure actions nationwide for 5 years because of the improper handling of loan servicing by Farmers Home. Congress took action in 1987 that resulted

in the end of the injunction, and then further tightened and improved the farm loan program in 1990.

Still, deficiencies in loan servicing and appeals procedures and protracted lawsuits by big borrowers carried beyond the 1980's and into the 1990's. Secretary Espy found a bureaucratic and legal morass at his doorstep when he took office.

I am impressed that the Secretary decided to get to the bottom of this and try to resolve the large loan crisis once and for all. The commercial banks and the Farm Credit System, after all, were able to successfully address their problems with large farm debts years ago.

Last March, the Secretary declared a moratorium on foreclosures to give him time to figure out how to effectively collect on delinquent debts. He ordered a major analysis by Farmers Home and the Office of General Counsel. He wanted to know how to prevent this mess from ever happening again, and how to collect the billions owed on delinquent farm loans. I'm sure that Michael Dunn will report to us on the status of that effort today.

I must say to the Department today that the time has come to lift the moratorium, to figure out a better way to do business, to ferret out the hidden assets of wealthy, dead-beat farmers and to collect every penny that can be collected.

I am sick and tired of reading stories about part-time farmers living in $800,000 condominiums, developing golf courses, and running big non-farm businesses when they owe Farmers Home millions of dollars. I am sick and tired of frivolous, time consuming appeals.

I know that small, hard pressed farmers in Vermont—too many of whom endure waiting lists to receive limited Farmers Home credit—would be sick and tired, too. These are the real farmers that Farmers Home was created to assist with supervised credit.

They live along rocky hillsides, not oceanside vistas. They drive tractors—often very old ones—and don't fly vintage airplanes. They don't have lawyers on retainer, but hire them only when absolutely necessary. They milk Holstem and Jersey cows—not Federal farm credit programs.

If the Secretary needs legislative changes to collect this debt, I expect that Administrator Dunn will tell us. We could probably pass the bill today.

I look forward to a detailed report on how this problem was created in the first place, how it spun out of control, and how it can be fully resolved. Thank you.

STATEMENT OF SENATOR THOMAS A. DASCHLE

I would like to begin by welcoming Mike Dunn, the Administrator of the Farmers Home Administration, to today's hearing. I have known Mike a long time and have enjoyed working with him over the years on agriculture policy.

I think it's only fair to point out that the very serious issue we are discussing today was not created on Mike's watch. As Farmers Home Administrator, he will, I am confident, be instrumental in correcting it.

In any event, I'm glad you are here, Mike, and I look forward to hearing your response to last Friday's *Washington Post* article that focused on a number of exceptionally large and delinquent FmHA loans.

I would like to make it clear at the outset that I am very disturbed about the loans discussed in the article. FmHA should never have made those loans in the first place, and I stand ready to take any legislative steps necessary to enable FmHA to collect on them.

Those delinquent loans are an embarrassment to FmHA, and, if not placed in the proper perspective, give the whole agency a bad name that it does not deserve.

It is essential for us to remember that the loans discussed in the *Washington Post* article were all made over a decade ago. They represent a time when FmHA had strayed from its core mission of helping family farmers establish their operations and make it through difficult times.

Today, there are restrictions on loan size and regulations that permit loans only to legitimate family farm operators. Therefore, the loans in question could not be made today.

While the *Post* article highlighted an abuse that should not be tolerated, some may deduce from that account that government policy is too lenient toward our Nation's family farmers. Nothing could be further from the truth.

No one works harder than true family farmers. They make up the fiber of rural economies and communities across the Nation, and form the bedrock of the Nation's food supply. It should be a priority of government to help them to weather tough times and continue growing.

Our family farmers chronically face tight credit and, as last year's floods illustrated, are all too frequently the victims of devastating natural disasters. Without the credit FmHA provides, it would be impossible for many established farmers to survive difficult years and prohibitively expensive for new farmers, particularly young beginning farmers, to establish their operations.

In recent years, FmHA has been moving in the right direction by only allowing family farmers to receive FmHA loans. It is our obligation in Congress, and that of USDA policymakers and administrators, to ensure that the Agency never again loses sight of its mission.

I hope we move quickly to recoup the taxpayer's investment in the large corporate entities and partnerships detailed in the *Post* last week, and tighten up protections to ensure that this sad chapter is U.S. agriculture policy is not repeated. I also hope we can all agree not to allow a few decade old examples of bad loans to hinder FmHA's efforts to carry out its important mission of helping America's family farmers.

Senator CONRAD. Thank you, Mr. Chairman. Thank you very much for allowing us to hold this hearing on such short notice.

The day I read that news article in the *Washington Post*, I immediately went to the Chairman and the ranking Member, Senator Leahy and Senator Lugar, and asked the Chairman if we could hold a hearing, if we could do it immediately. As always, he was very gracious in saying if you can put it together, let us do it, it is important that we do. I went to Senator Grassley, who is the ranking Member of the subcommittee, who also agreed that we ought to act quickly.

I also want to acknowledge my colleague Senator Kerrey of Nebraska for any statement that he might want to make.

STATEMENT OF HON. J. ROBERT KERREY, A U.S. SENATOR FROM NEBRASKA

Senator KERREY. Thank you, Mr. Chairman.

I would just say that it seems to me, Mr. Dunn, this is a situation that far too often gets repeated. I know that this particular expose was brought to our attention by the *Washington Post* first, and then as a consequence of Senator Conrad's diligence, we are now here.

I suppose we will act sort of collectively as the local priest, and at some point we will tell you to "Go and sin no more," and we will tighten up and we will try to give you authority to go after, as Senator Leahy said, some of these deadbeats who are ripping off the taxpayers.

I say, Mr. Dunn, that the taxpayers are going to have to cover this loss. That is what happens here. Once again, I am going to have to go to my taxpayers and say we are going to pass the hat, and your hard-earned income, your sales tax, your income tax, or whatever tax we use is going to be collected to pay these losses. That is essentially what we are doing.

It calls into question this whole effort, it seems to me. It truly does. I know there are political pressures that make it difficult for the Farmers Home Administration to act in a responsible fashion. For example, I might come to you and say, "Gee, don't foreclose on this individual, because he happens to be a farmer in Nebraska, and he has made his case to me, and he or she has appealed to me and, gosh, I don't want the foreclosure to occur." So I come and say I support a moratorium. You have got political pressure that makes it difficult.

Most importantly, it seems to me, Mr. Dunn, any time it is not our money, it is difficult to do risk assessment. It seems to me, as I look at what the Farmers Home Administration does, we are performing many of the functions that the private sector lenders perhaps ought to be doing. I just say that, on behalf of taxpayers, it does call into question this whole effort.

It may be that there is a better way for us to provide capital, allowing the lender to do the risk assessment and carrying the burden of that risk, and keeping us out of it an awful lot more, so the political pressure does not cause us to take action that produces this enormous loss.

That is a frightening number there. If you add all that up, that is an awful lot of money that the taxpayers are on the hook for. You see, the commercial lenders run their losses down. The Farm Credit System did, as well. The life insurance companies did, as well. It is only the taxpayers that continued to run up these large loan losses.

That is an awfully big number there, Mr. Dunn. I am just saying, Mr. Chairman, it calls into question not just the need to go after these people that are cited in the *Washington Post* that we will be able to identify, but it calls into question whether or not we are doing this whole program in the right way, whether, with political pressure, and when it is not our capital at risk, we are ever going to be able to get to a point where I can look the taxpayer dead in the eye and say "Don't worry, we are not going to have another one of these situations somewhere down the road 4 or 5 years from now."

Senator CONRAD. I also want to thank ranking Member on the subcommittee, Senator Grassley, who is here, and recognize him for any opening statement.

STATEMENT OF HON. CHARLES E. GRASSLEY, A U.S. SENATOR FROM IOWA

Senator GRASSLEY. Thank you very much.

The *Washington Post* recently highlighted loans made to farmers in Kern County, California, under an old emergency loan program. A little over 14 years ago, in a November 8, 1979 hearing, before this subcommittee held by Senator Ed Zorinsky. He referred to a *60 Minutes* segment about an unnamed person in Kern County, California, who received $15 million in disaster loans. Senator Zorinsky also noted that, in 1 year, the Kern County FmHA made 206 emergency loans worth a total of $205 million.

Of course, you do not need a calculator to do the math on that one.

Clearly, the loans were generous, and apparently not too difficult to receive. Unfortunately, the *Post* did nothing to dispel the perception that Farmers Home continues to this day an easy money policy available to all farmers, regardless of need.

Now, in Washington, as all of us know so well, the perception of an issue all too often is vested with a reality which ignores the truth, and a front-page article in the *Washington Post* gives an issue a legitimacy which may be difficult to refute, regardless of how compelling the full story may be.

The *Post* article undoubtedly left the impression that Farmers Home serves only the well-to-do and serves them all too well, as witnessed by the untold billions still uncollected. The reality, however, and as we all know on this committee, is very different. Vested with the title "lender of last resort," Farmers Home Administration is legally, and rightfully so, entrusted with the unglamorous job of assisting those who are turned down for commercial credit. Yet, no one here doubts the importance of their work.

In Iowa, for instance, Farmers Home has a loan portfolio of $1.2 billion, providing 6,400 direct and 4,600 guaranteed loans. With respect to the emergency loans in question, Iowa has just two of these loans, one made originally in the amount of $500,000, the other in the amount of $900,000.

Both loans have since tripped the $1 million figure, only on account of the interest build-up during the *Coleman* moratorium, and because of a counterlawsuit. One has just been settled, and the Farmers Home Administration is in the process of closing it out. The other is now going through foreclosure, with the Farmers Home Administration prepared to pursue a deficiency judgment against other assets.

Now, there is no need to be specific about my State, but the point that I would like to emphasize for my State, at least, is this: Out of 10,000 Farmers Home loans, there are only two outstanding emergency loans, and that is out of a portfolio of $1.2 billion, including guarantees. So there is a little over $2 million in these loans out of that $1.2 billion, and both are in the process of being settled.

I hope that by the hearing that we are having today, we will come to an understanding of why these loans authorized in 1978 are still uncollected almost 15 years later. More importantly, I also hope that, by this hearing, we can identify future problems that might ensue and begin to consider measures that may be necessary to nip those future problems right now.

To be sure, we should treat the *Post* article with the utmost seriousness, but we must not lose sight of the fact that the vast majority of borrowers are farmers who rely on Farmers Home, as a source of operating and ownership loans. Just as important, we should not forget that the American farmer historically has had an outstanding record of resolving to repay his just debts. His ability and willingness to repay his debt is a reputation well deserved and hard-earned.

I thank you, Mr. Chairman.

Senator CONRAD. Thank you, Senator Grassley.

Mr. Dunn, if I could, I would like to ask you a series of questions and then turn to my colleagues for their questions, as well. First, could any of the loans described in the *Washington Post* article be made today under current law?

Mr. DUNN. No, sir, they could not.

Senator CONRAD. At what point were the programs killed or sharply curtailed that permitted loans of this nature?

Mr. DUNN. Senator, if you will, there was decade-long series of oversight by this committee and the House committee looking at

these, and at various points in legislation, in the Congressional Act of 1985, again in 1987 and in 1990, these have been tightened up.

Senator CONRAD. So we are assured that this cannot happen again, nobody can walk in and get an emergency loan based not on their ability to cash flow to pay that loan back, those days are over with?

Mr. DUNN. That is correct, Senator.

Senator CONRAD. That leaves us with the underlying question of those that are still out there delinquent, where at least in over 600 cases there is substantial collateral. As I hear your testimony, you are assuring us that each and every one of those cases is being pursued aggressively. Is that the case?

Mr. DUNN. Yes, Senator, they are.

Senator CONRAD. As your testimony relates it, my understanding is that you have told this committee that within 12 to 14 months, you will resolve to the extent possible, given legal considerations, all of those outstanding cases?

Mr. DUNN. That is our intention, Senator.

Senator CONRAD. Let me as you this question, because I think it is perhaps the most important question we need to get answered today: Are there legislative initiatives that this committee and the other committees of Congress need to take that would assist you in pursuing those that are currently delinquent?

Mr. DUNN. Senator, I have outlined a couple of instances in my testimony. I have worked with our staff and they have submitted to me a group of legislative proposals. I have discussed this with the Secretary, and he has told me to hasten forward to work with you and the House Members to come up with a package that will assist us in resolving these issues.

Senator CONRAD. Could you tell the committee what would be the most important steps that we could take that would be of assistance to you?

Mr. DUNN. One of the major problems that we have is as a result of other pending cases, criminal cases. There does appear to be a backlog in Federal court, and on many of these cases the regional attorneys are saying, look, there is no collateral left here, there is no reason for us to pursue some of these actions.

So what we would like to do is get the authority similar to what we have with our single-family housing authority, where we can contract with the Office of General Counsel or private attorneys to pursue these matters on behalf of Farmers Home Administration and the U.S. Government.

Senator CONRAD. Have we absolutely assured ourselves and assured the taxpayers of this country that we have made a full investigation of the assets of these what I would classify, as the Chairman did, as deadbeats?

Mr. DUNN. We are in the process of that. As I indicated in my testimony, we have contracted with asset investigation groups throughout the country to find out where there has been conversion of these assets that had been pledged to the Federal Government. Where we find abuse, we turn that over to the OIG and turn it over to Justice to pursue criminal actions, as well.

Senator CONRAD. Can you give us a time frame for your specific legislative recommendations on things that are necessary to help you pursue those who have not paid who have substantial assets?

Mr. DUNN. Senator, just as soon as you and your staff would like to get together with us, we would be willing to work with you to put together a legislative package that would help us out.

Senator CONRAD. I think we should do it today. I think we should start today. It is just intolerable I think to everyone in this country that people benefited from government programs that were ill-devised at the time they were put into effect, and people have abused the privilege of receiving assistance from their fellow Americans, and even now though some of them still have substantial assets.

Obviously, it is another issue for those who do not have any assets remaining. Yet, those that do have substantial assets, for them to duck, to hide, to be living in what can only be described as splendor and to have substantial assets—I mean to read about somebody having a $1.7 million office building and somebody living in a $900,000 beach condo—and have debts outstanding that they are not paying that they received more than a decade ago, I think is enough to anger anyone.

I would turn to Senator Lugar for questions that he might have.

Senator LUGAR. Thank you very much, Mr. Chairman.

Mr. Dunn, in your testimony you pointed out the reforms that were made in the Credit Act of 1987. Most of us around this table participated vigorously, including yourself, in that situation. On review now, you point out it should be noted that the appeals process provided much needed objectivity to ensure borrowers' rights. Indeed, that was a major focus of the group here.

However, it inadvertently provided opportunities to significantly delay the foreclosure process. For instance, if a borrower exercised all servicing appeal rights, the process could continue for 1,200 days, which you have illustrated in Attachment 8[4] as to how that might go on.

That strikes me now, as it did then, as too long. We had considerable argument during those days, as you remember, about the borrowers' rights situation. It is a fine point in terms of equity for the individual farmer and, likewise, some reasonable process for trying to gain repayment and foreclosure, if that is finally required.

In the package of legislative thoughts that you have, have you thought about restricting the 1,200 days? In other words, is it not, as a common sense matter, important to address the very point you made on page 12, to get to a different situation here?

Mr. DUNN. Senator, I agree with your concerns here, but I also understand the need to protect the rights of the individuals that they might have.

I think what we would come to you and talk about are some other areas that may help us much better in this appeals process arena. For instance, the use of administrative law judges for these large loans would really help, because you would have somebody who knows the law more and is going to be more judicious, based

[4] See Appendix, page 45.

on what is presented to them, not what some accountant or attorney comes in and represents as to these large wealthy borrowers.

A second area is maybe grouping those. It is not unheard of for these borrowers to have a half dozen appeals going simultaneously, and unfortunately not to the same appeals person. So we would also say they should all go to one, so that there would be one body of evidence and it could be ruled on much quicker, and there would be less of an opportunity of having judgments or appeal decisions that are opposite of each other.

So those are the types of things that I think we can work together to institute in here on an appeals process and a revision of that. I know the Chairman here is working very diligently on putting together many of these types of things that would allow us to still provide the rights to the borrowers, but ensure that the Federal Government also has its rights.

Senator LUGAR. I commend you on those constructive views. Let me just say that the Chairman and I during this period frequently debated these issues. I have great respect for the feelings that he has had about that and often have been persuaded. I think both of us have a common view today, and that is this is running amuck. This is unconscionable. I say this not just with regard to these people we keep talking about with regard to the villas, the yachts and so forth.

My impression is that with small borrowers, all the rest of them not being mentioned today, that some of the problems of collection and foreclosure and what have you are going equally poorly. In other words, before we all get exercised about these people who own the yachts, we have got to remember that there are tens of thousands of cases here, and a situation that strikes the normal American, looking at common sense, to say that this is a very, very special group of people.

Of course, farmers are. This is one factor we look at. We try to think, as advocates of farming, of how we can help people, as you have pointed out today. However, at some point, our bending over backwards to help the small farmer has also created a situation with the large farmer or with anybody. In other words, we have got something that is stretched out I think in a common sense way far too long.

Now, if we are not able to clear this up, I think the Chairman of the subcommittee and I both come to the conclusion that the American people's tolerance for all of this will likely be limited.

This has been an inside game in the past, and we have been trying to argue in behalf of each other of how we could sort of keep it alive without anybody knowing the difference. Now people do know the difference. We are going to be writing off billions of dollars. We have already written off $10 billion, as you say, just in principal, $13 billion in interest. That went down to the deficit. This is real money with regards to the budget battles we are having elsewhere.

We cannot meet in this room as sort of a closed society and somehow, out there when we get into the deficit problem, pretend it does not exist. We are going to inherit this, as you pointed out, some of this is going to be written off, as Senator Kerrey said, to the detriment of the American people, real taxpayers.

So my own feeling is we ought to get into the legislative program, but we really ought to take a look at the totality of the picture, because what also is intended to help the small has also helped the big and may not have been right for either one of them in terms of good management.

In the past, your predecessors were burdened by a committee which was hammering on them to go slow, to forget, to omit. Now you are faced with a committee that I hope that has taken a 180-degree turn and really wants a good bit more rigor with regard to all of this, for the sake of having the problem.

Now, just as a matter of philosophy, because this is sort of fundamental, you pointed out correctly that you make loans to farmers, but you also counsel and teach them, help them with credit and what have you, and that is important. Yet, I wonder, are there good criteria to begin with for making these loans? In other words, you are not operating a charity. These are not grants. They are meant to be loans to help people who cannot get credit elsewhere, always a risky business.

We cannot get into everything today, but I just wonder about the general philosophy, how many people are there who are in this situation presently? In my State, the number of people in farming at all has decreased substantially, and that has been true across the board. The number of people who are having credit problems we know, we can identify them almost by name.

I think we are going to come down to justifying the continuation of this whole business at some stage. It may go by the board because it was badly run in the past—not now, but in the past—but even then I question in my statement why Secretary Espy has had this moratorium at all this time. I am grateful he is going to end it. I do not think it should have happened to begin with. I think it sent the wrong signal in terms of leniency. That may not have been what he wanted to do, but that was the signal that went out there, and it needs to be cut out, if not this week, next for sure, so we get back into the regular business of collecting, without any questions being asked.

I throw all of this out, because this is sort of our first oversight hearing. It comes at an unfortunate moment, but maybe the *Washington Post* article was a good spur to sort of get our situation reformed.

Mr. DUNN. Senator, if I can react to some of your thoughts there, because I find myself in agreement with a good number of things that you have outlined here, but philosophically may be approaching them just a little different.

There has been a lot of talk about this is criminal and these types of actions border on criminal activities. I think what would be criminal is if me, as the Administrator, did not learn something from this and did not adjust the way this agency operates and the clientele that we target for, and ensure that we do still service that strata of borrower that you and the other Members of Congress have said this is the law, you are to provide them with this assistance.

If I did not ensure that the Farmers Home employees did everything within their power, that when that first borrower walks in

that door, that our goal was to graduate that borrower to the private sector as soon as possible, but to assist them in developing and molding that person as a farmer in the future. Your example is typical. That is the type of legacy that I believe the Clinton administration and the Farmers Home employees want to leave.

You talked about a bit about the whole appeal process and then about the suspension of the loans. Again, it would be criminal, if I did not take a look at what we learned from that process out there. In 35 percent of those loans reviewed, we did not follow our own procedure. That tells me that there is still a need for the appeals process out there, because a third of the time we are not doing it right.

My job, it is incumbent upon me to make darn sure we do it right in the future. That again is what we learned from this appeals process. We analyzed it, where were the common mistakes, what happened to us, where did we go wrong. We developed from that a checklist of 21 different items, common items of where we made mistakes, and that will sit right in front of that county supervisor, as they go through this process, so that long period of delay that you point out will not exist. We will do it right the first time, and we will get it right and we will go forward with it.

We also looked at who were these loans that came in. This is very important in the context of today, because 40 percent of those loans that we looked at that got in trouble were the result of some natural disaster that got us going there.

So what we did, before we developed folks to go out and assist farmers in the current natural disaster we have, the drought in the Southeast and the floods in Iowa, we have come back and done a complete retraining. We have rearmed these people with laptop computers and put the program in there so they can run out to see if these programs are going to pay back, if they are going to cash flow. Those are the types of things that we have learned. It will save us billions in the future, I am sure. It would be criminal if we did not learn from what we have done in the past.

Senator LUGAR. I congratulate you on those reforms, and that is encouraging. In subsequent appearances, you will be able to tell us, I suppose, how it has taken and what kind of good news there is from the changes you are making.

Let me just ask this final question: Are the holders of the large loans that we are talking today still eligible for any Farmers Home loans, and have any additional loans been made to these individuals that we are chastising broadly today?

Mr. DUNN. They would not be eligible, based upon the criteria that we have. Let me double-check with some of our people, so I do not give you a wrong answer.

They are not eligible for any type of new loan programs that we have eligible today, that we have on the books today. They would be eligible for some type of restructuring of that present loan.

Senator LUGAR. I did not mean to ask the question as a trap or what have you. My staff has had some information that there may be eligibility in some loans that have been made. I would like to work with you on that, because clearly, if we are going to get into the legislative process, we want to stop the loopholes. While we are broadly condemning all this crowd, if for some reason we are still

loaning money to them, that would be unconscionable, also, and I would like to cut it out.

Mr. DUNN. Senator, we will diligently research that, and if we find something different than what I have told you, we will let you know.

Senator LUGAR. Thank you.

Senator CONRAD. Could I just rivet on that point? What I hear your testimony to be is they would not be eligible for any additional loans, but they would be eligible potentially for restructuring?

Mr. DUNN. That is correct.

Senator CONRAD. Even there, would they not be limited in the amount that could be restructured? Would they not be limited by the $300,000 cap?

Mr. DUNN. Yes, they would be.

Senator CONRAD. Again, it seems to me in some sense we are dealing with the past here in that the loans that were made are no longer are allowed. Yet, we are still living with the problem of people who had those loans made to them more than 10 years ago, that we are not collecting on or so far have not collected on.

I think the thing that bothers me, my own anger level, the most are people that have substantial assets and are not paying what they owe. Number one, I have to wonder about what kind of people they are. I find it amazing that people can go to sleep at night, when they have had loans made to them and they have assets and they do not pay what they owe. It says something about basic character of people.

Is there anything you can tell us about those over 600 borrowers who owe over $1 million, who have collateral? What is being done and what will be done in the coming days to absolutely assure ourselves that every nickel that can be recovered will be?

Mr. DUNN. I think, Senator, as I have outlined in my testimony, the development of our Large Loan Group in Washington, the training that we are providing the people in the county, the contracting with the investigation group to find out where the assets are, if there has been conversion, those are the type of things that are going to assist us in determining what is out there and what we can go after.

Obviously, we are going to overlook things. The types of people that we are contracting are former FBI employees and, as a tax collector, you are well aware of the type of folks that we are engaging to assist us in assuring that we get every cent that is due the Federal Government.

Senator CONRAD. One other point I think should be made: Would it not also be true that none of these people could be restructured, if their delinquency was as a result of something within their control?

Mr. DUNN. That is correct.

Senator CONRAD. They could only be restructured, if the delinquency was beyond their control. When you have people who have assets, obviously the delinquency is within their control.

Mr. DUNN. Senator, there were two issues that you and Senator Cochran and Senator Lugar had debated quite a bit, and that was the bad-faith provisions and beyond the control

of the borrower, and those provisions in this current legislation does give us a big stick.

Senator CONRAD. I think we need to make that point. Let the word go out that there is law that is available, that is on the books that will allow us to go after those who refuse to pay what they legitimately owe.

Let me ask you one final question and then turn it over to Senator Grassley. Do I need to call Attorney General Reno and ask her to put more resources on criminal investigation and criminal cases against people who are refusing to pay?

Mr. DUNN. I am tempted to punt and give this to Ms. Luken.

Ms. LUKEN. Senator, I do not think either Mr. Dunn or I are in a position to give you that advice. In all instances where the Farmers Home Administration and the General Counsel's Office and the Inspector General's Office have interacted with the Department of Justice, of course, we believe the Department of Justice has vigorously protected the government's interest in these cases. I am sure that the Department of Justice will hear the results of this hearing, as will the Farmers Home Administration, and the Department of Agriculture, and I am sure that they will hear what you are saying about what importance you place on the prosecution of these cases.

As for my part, I certainly will disperse the results of this hearing down to the field attorneys in the general counsel's office, so they understand the importance this committee places on following up on these cases.

Senator CONRAD. Let me just say, in response to a remark that the Administrator made about the reaction of attorneys about there not being collateral, that what deeply concerns me is that there is collateral out there that has not been discovered. I am very pleased to hear that you have identified investigative teams around the country that can pursue the existence of those assets.

I have learned from past experience how those assets can disappear, and that should not be permitted. Let this word go out—if there is conversion, they are going to be pursued and they are going to be held accountable, because these people were made loans that came from the money of other people in this country. They ought to be held accountable, and they will be.

Senator Grassley?

Senator GRASSLEY. In the late 1970's, the Office of Inspector General, at the USDA, in reviewing these cases and making recommendations, said that there were certain safeguards that were in place to make sure that borrowers were qualified and that their losses were not being verified, The OIG report stated that these safeguards were not being followed.

I do not want to ask a question just about these safeguards, because I think you have assured us that you are taking, or even previous Farmers Home directors have taken procedures to make sure these are solved and safeguards followed.

But, generally speaking about the recommendations of the Office of Inspector General and what they recommend needed to be done, do you feel that those recommendations were good recommendations, and that there has been administrative or legal statutory action taken to make sure that those recommendations be followed?

Mr. DUNN. Senator, there have been a number of investigations of Farmers Home Administration on these loans and other loans, on how we do our business down there, and recommendations from auditors, the General Accounting Office, as well as the OIG.

Personally, what I have found is that we seem to be investing a lot of resources, both human and fiscal, in helping these auditors continue to tell us that we have a problem. I know we have got a problem. What I want to do is a quantum leap to get out ahead of it, to fix that problem and start directing our resources at that.

So we are working with them in a number of different areas. I think we have a very good relationship with the OIG at this time in assisting us in some investigations. Again, their resources are limited.

There will probably, as long as there are administrators and as long as there are auditors, there will be differences about how we best ought to proceed on things. In general, I agree with 90 percent of the recommendations.

Senator GRASSLEY. Quantifying it probably answers the question, but let us just go not so much to substance, but to the process of certain recommendations and I assume I am talking more about the Inspector General, but there are other people making recommendations.

Do you have a procedure—and if it is different than procedures prior to your taking over, make that clear, too—are there procedures for at least consideration of all recommendations and a decision-making process that brings you to a point that, yes, these recommendations should be followed and these should not be followed, as opposed to just being lackadaisical about these sorts of people, on the outside, that are making recommendations and kind of a feeling—"Well, I do not really have to give them much consideration, because maybe their track record is not too good as far as you are concerned, or your agency might be concerned?" I am at a thought process here within your agency towards recommendations.

Mr. DUNN. Senator, I am very open and receptive to recommendations. Let me give you one that is a little different than this subject and explain some of the difference that I might have, and that is in the area of housing. There have been recommendations that we ought to have centralized servicing in housing and go to some type of escrow account. We currently do not escrow.

I have looked at this problem, and one of the recommendations was to sell off another batch of our good loans. I do not think it is my fiduciary responsibility to protect every asset we have in the Government. I do not think discounting loans 50 percent or better and selling them off to the private sector is in the best interest of the government, if we can do those same types of centralized services in-house. So we are proceeding now on developing an escrow account at our accounting department, so that we can provide those types of things that we did not have in the past.

So I am receptive, when people point out what a problem is, but I am not always receptive that they have the single best answer.

Senator GRASSLEY. My question did not imply that you ought to agree and institute changes based upon every recommendation. I guess I would like to know—and I do not think you have answered

this yet—whether or not there is a process by which you make a judgment that these recommendations are good and those are bad, and I assume the ones that are good are going to be implemented. Do you have a process that you——

Mr. DUNN. Yes, we do, Senator. We do sit down and we meet with them. Many of the procedural changes that we have made and I have outlined in my testimony, in fact, did come from OIG types of audits, so we do on a regular basis meet with them. We take those audits seriously and we try to the best of the resources we have to alleviate what we feel is the core root.

Senator GRASSLEY. You discussed with Senator Lugar about graduation. Obviously, the term "graduation" did not mean much during the time that these loans that made the headlines were under consideration. There was even some indication that there was not much of a process towards graduation. You have indicated that that is your goal.

Now, in regard to these specific people getting loans, they could not get loans today. Things have been changed. Are you satisfied that that process takes into consideration that the ones with the—I suppose it would be based upon the highest worth that they have, as opposed to those with lesser worth—are being prioritized, to make sure that those that are at the—even though they still legally qualify for Farmers Home loans, that the ones that would be least in that priority list are being reviewed, to make sure again a decision being made as to whether or not they should graduate or not graduate on an individual basis?

Mr. DUNN. Yes, Senator, on these particular loans, where we would graduate them from is liquidation or getting them out of our system, if at all possible.

Senator GRASSLEY. Pardon me. I am not talking about the loans that made the headlines. I am talking about under present policy and the principle that you espoused to Senator Lugar on graduation, your total commitment to that, to get them out of the Farmers Home system into the commercial system. Are they being reviewed on the basis of those that would tend to have the least need, as opposed to the whole pot?

Mr. DUNN. Absolutely, Senator. That has been a priority of this administration, of me as the Administrator. I do not want those loans in our portfolio that ought to be in the Farm Credit System or in commercial banks. That is not what you passed the laws for us to help. You passed the laws for us to help that strata that is right below that, and we are going to do everything we can to get those types of loans out there.

Oftentimes, when you get a report like this, what an agency will do is to try to get better loans on the books. That is not what you have charged us to do in the law. You have charged us to help that strata below that and help them work their way up to be better loans.

Senator CONRAD. We will have to suspend and recess for 15 minutes, because we have a vote on the floor.

[Recess.]

Senator CONRAD. The hearing will come back to order.

A couple of things that I think should be clarified that would be important for people to know. With respect to the 1,200 days for appeals, actually only 510 days of that would be because of the appeals process. Isn't that the case? You have two 255-day appeals; the rest of it are other servicing matters that are available. Wouldn't that be the case?

Mr. DUNN. That is approximately correct, Senator. We have included in your packet of information for everyone's edification on the appeals the appeals process chart that has been provided to us by the FLAG folks, and it makes for interesting reading and gives you the idea and time frames within that.

Senator CONRAD. Let me just say that my independent appeals legislation, on which Secretary Espy was the lead sponsor on the House side, would dramatically cut the time for those appeals from 255 days for each of the appeals to 135. I think that is important legislation. In fact, I just visited with Secretary Espy about it in the last week in terms of his overall government reorganization plan for USDA, and hopefully major parts of that independent appeals process will be adopted as part of an overall reform.

One other point of importance to make is the *Washington Post* story that, I think, perhaps is misunderstood, stated that there are no graduation deadlines. In fact, there are graduation deadlines in current law. Is that not the case?

Mr. DUNN. There are deadlines in the new beginning farmer law that was recently passed, Senator, that gives us a certain time period to work with those farmers to ensure that they are graduated to private credit.

Senator CONRAD. My recollection is that those deadlines are 10 years for direct operating loans and 15 for a combination of direct and guaranteed loans?

Mr. DUNN. For those taking part in that program, that is correct, Senator.

Senator CONRAD. Any other points that you would want to make before we close the hearing? Any other things that you would want this committee to be aware of?

Mr. DUNN. I would just reiterate, Senator, that this administration, the Clinton administration, the Espy Department of Agriculture, we are all concerned about the protection of the taxpayers' dollars. That is what we are about on reinventing government. We also are going to do that with the compassion, and the understanding, of a Federal Government that will faithfully implement the laws of the Nation, and the wisdom of Congress has given us programs to administer, and we will do so.

Senator CONRAD. Let me just close by saying again that I want to commend you for not only producing a voluminous report to this committee—I last night was able to read through everything that had been delivered by last night, and it really is very, very good work and very, very helpful to this committee. I want to commend you publicly for, in a very short time, turning around this amount of information to the committee. I also want to commend you for outlining an action plan to go after these folks, these large borrowers with million-dollar loans, who have assets, and who are failing to pay. It is unconscionable that they fail to pay.

I just spoke to Senator Lugar as we went over to the floor together. Growing up in small-town North Dakota, the thought that people would have gotten these loans is disturbing. It is one thing if everything turns against you and you have no ability to repay. That is one thing; but that these folks have substantial assets, and have not repaid, reflects very badly on them and their character.

There is no excuse. There is no excuse for failure to repay what you owe if you have the ability to do so. That is fundamental. That is a test of basic character. I hope the word goes out from these hearings. I hope it goes to those who are advising some of these people. Because there is going to be zero tolerance—zero tolerance in this committee for people who have the ability to repay and fail to do so. That is unacceptable.

Again, I thank Mr. Dunn very much, Ms. Luken, for your appearance here today. Again, my thanks for the swiftness of your response. Yes?

Mr. DUNN. Senator, I will accept that commendation from you on behalf of the men and women who work at Farmers Home Administration who have put in long hours in advance of this hearing trying to do the right thing and faithfully carrying out the programs of this Nation. I thank them for the hard work they did in the last week to do the research so that we do have that information there. Yet again, a lot of it was not far away. We have been working on it.

Senator CONRAD. We appreciate it very much, and I also want to thank those people. I know they must have been burning the midnight oil to produce the very excellent testimony and the work that had been prepared for this committee.

Thank you very much.

[Whereupon, at 11:55 a.m., the subcommittee was adjourned.]

limit or prevent their success. Unfortunately, in the past, FmHA has gotten away from providing supervised credit as the Agency's focus shifted to larger, wealthier farmers. *Those days, however, are now over.* Our state directors are aware that supervised credit is one of the Clinton administration's top priorities, and efforts are already underway to provide training to employees to accomplish this goal.

Large Delinquent Loans

During the Clinton administration's tenure, FmHA's focus will be to provide skillful assistance to small, limited resource farmers. Unfortunately, there remains at this time, the unresolved backlog of large delinquent loans left over from the past decade when large, wealthy farmers were granted emergency loans. These were the subject of *The Washington Post* article.

The Washington Post article serves a very useful purpose. It sheds light on past policy decisions which have resulted in problems that had been festering in the Agency for years. These problems, which we have already discovered, demand prompt and decisive action.

My colleagues at FmHA have been aware of and concerned about the enormity of the outstanding debt which has been accumulated from delinquent large loans made years ago. Resolution of this situation was one of the first issues that I pursued after taking the oath of office on November 30.

Today's hearing provides the opportunity to bring you up to date on our recent activities with respect to the large delinquent loans, as well as the related foreclosure suspensions. In addition, we will cover steps which we are taking to return FmHA to its traditional mission of providing supervised credit to small and limited-resource family farmers and ranchers.

I cannot emphasize too strongly the Clinton administration's conviction that FmHA's mission to assist small, limited resource family farmers is paramount. This is the central mission which President Clinton, Secretary Espy, and I, as administrator, intend to see FmHA fulfill.

Foreclosure Suspension

I would at this time, like to comment upon Secretary Espy's suspension of foreclosures which has been in effect since March 5, 1993. Allow me to provide a brief summary of the effect of the suspension on the resolution of the large delinquent loans.

- On March 5, 1993, there were 4,833 cases in the foreclosure process. Of this number, the Department of Justice (DOJ) had 962 cases.
- Of the 4,833 cases in foreclosure, 240 were borrowers who owed more than $1 million dollars.
- In March and April of 1993, Secretary Espy mailed 3,913 letters to borrowers in foreclosure providing them with the opportunity to request a review at the Secretary's level to determine if their loans had been properly serviced before being submitted for foreclosure.
- Of the 3,913 farmers who received letters, 1,090 responded with a request for a review.
- Of the 1,090 borrowers who requested a review, 100 were borrowers who owed FmHA over $1 million.
- Of the 100 borrowers who were reviewed, 34 were sent back to the States for corrections in the servicing process.
- In California, six large loan borrowers requested a review by the Secretary's office. The review showed that all had been properly serviced, and the State was instructed to continue with foreclosure.
- *None* of the borrowers in *The Washington Post* article requested a review.

In summary, of the 100 large loan borrowers who requested a review, 66 were sent back to the States to proceed on foreclosure. Secretary Espy has indicated that he is in the process of finalizing his personal review of FmHA's findings and anticipates announcing the lifting of the suspension within a week.

Overall, this suspension served a very important purpose. In addition to guaranteeing the rights of those whose documents were reviewed, the suspension identified weaknesses in the foreclosure procedures that we can now correct.

A checklist of items has been developed for use in the field when the suspension is lifted (Attachment 1). The checklist addresses loan servicing weaknesses discovered by the review. This checklist will be used by District and State office personnel to ensure that all required notices have been provided to the borrower. It will also

APPENDIX

PREPARED STATEMENT

Michael V. Dunn

Good morning, Mr. Chairman, and Members of the subcommittee. Thank you for inviting me here today. I appreciate the opportunity to discuss this very important issue of the large delinquent farm loans in the Farmers Home Administration (FmHA) portfolio.

I want to say at the outset that the Clinton administration is outraged at the thought that wealthy individuals are not satisfying their just debts to the Government. This was exactly the type of situation that the President and Vice President set out to rectify as they sought to reinvent government. I pledge to you, as the President's representative, that we at FmHA will do everything humanly and legally possible to collect every dime that is owed to the American people.

Why It Cannot Happen Again

Million-dollar loans are no longer available from FmHA. The delinquent loans reported by *The Washington Post* were made under Emergency Loan authority. Amendments to the Consolidated Farm and Rural Development Act of 1980 (Public Law 96-438), gradually reduced the maximum emergency loan to $500,000 for any one disaster. This legislation also phased out the bonus annual operating and major adjustment loans. The Food Security Act of 1985 (Public Law 99-198), limited emergency loans to family-size farmers and prohibited loans to farmers eligible for credit elsewhere. Further, direct operating and ownership loans are now limited by law to $200,000; guaranteed operating loans are capped at $400,000; and guaranteed ownership loans cannot exceed $300,000. In all cases, the borrower must be a family-size farmer or rancher.

FmHA's Mission

Before I discuss the large delinquent loans, I would like to take a minute to share with you the Clinton administration's philosophy on the mission of FmHA. FmHA is required to provide assistance to only those farmers who are unable to obtain credit from commercial sources. Typically, our borrowers are family-sized farmers. Many lack production resources, such as productive land and modern buildings and equipment. Many also lack the personal resources, such as sufficient education and experience, which provide the foundation for management skills critical for success. We view it as our mission to assist these farmers in anyway possible not just to get credit—but to become credit worthy, successful farmers.

Supervised Credit

That is why I firmly believe that we must provide supervised credit for these borrowers. This involves working closely with borrowers from day 1 to nurture, teach and counsel them. This is accomplished through frequent and thorough monitoring of the borrower's farm production and financial management to pursue strategies that develop actions necessary to achieve the customer's planned objectives. Thus, farms receive technical assistance as well as individual counseling and evaluations necessary to focus corrective measures on the specific factors that might otherwise

document that all required servicing actions have been completed prior to acceleration and/or foreclosure of all direct farmer programs accounts. Accounts previously reviewed by the Office of the Secretary and returned for liquidation will not be subject to this review.

Current Status of Large Loans

The large loans referred to in *The Washington Post* are, indeed, a problem to FmHA. They will be a significant drain on the U.S. Treasury. It is apparent that some of the loan funds in question may never be recovered.

There are currently 971 delinquent large loans—that is, loans of more than $1 million. The total principal and interest outstanding on these large loans is $2.2 billion (Attachment 2). The average loan size is $2.3 million. One hundred ten of these loans, valued at $562 million, are in California.

The large delinquent loans should be considered in the context of the entire FmHA portfolio. Currently, there are 136,050 FmHA borrowers, of which 1,030 (less than 1 percent) were million dollar borrowers (Attachment 3). These million dollar borrowers comprise almost 40 percent of total delinquent principal and interest, (Attachment 4)[5], but only 3.5 percent of total delinquent borrowers.

The typical Farmer Program loan stands in stark contrast to this portfolio of large delinquent loans. In 1993, the average farm loan was $75,106 and was provided to a farmer with assets of about $313,000. The average family living expenses for the farmers receiving direct farmer program loans was only $17,000 (Attachment 5)[6].

On the other hand, over a decade earlier, million-dollar loans were made to large corporate entities and partnerships, which, among other things, refinanced existing debt from commercial lenders. The principals in these entities were often wealthy individuals with numerous nonfarm business interests such as real estate development. The loans were not underwritten by cash flows, rather by assumed property values and projected increases in property values. When property values collapsed, the security of the loans collapsed as well.

Background on Large Loans

NATURAL DISASTERS

When many large loans were made, several parts of the country including California, had experienced a series of natural disasters. First, there was a severe drought in 1976–1977 affecting States in several regions. When the rains finally came in California, there was extensive flooding. Farms were deluged. Shortly thereafter flooded farmers from California, and drought-stricken farmers from the South and other areas, turned to FmHA for help. Thus, the large emergency loans were made. The genesis of these loans was for emergency assistance.

ECONOMIC SITUATION

Following this series of natural disasters, U.S. farmers were plagued by severe economic problems. The value of farm land dropped precipitously, and commodity prices collapsed.

The total value of farm assets decreased from just under $1.1 trillion in 1981, to about $850 billion in 1986 (Attachment 6)[7]. Total farm equity decreased from $910 billion in 1981, to $681 billion in 1986—a 25 percent decrease. Interest rates averaged 12.87 percent during most of that period, and peaked in 1981 at 18.87 percent. At the same time, the value of agricultural exports decreased from $43.3 billion in 1981, to $26.2 billion in 1986—a 40 percent drop. These factors combined to create a crisis in the agricultural sector which caused all lenders to experience severe losses on their agricultural portfolios.

Between 1985–1986, the Farm Credit System, commercial banks and life insurance companies all took huge losses. Losses to commercial banks peaked in 1985 at $1.3 billion; losses to the Farm Credit System peaked in 1986 at $1.3 billion; and life insurance losses peaked in 1986 at $827 million. FmHA losses, however, did not peak until 1989 when FmHA lost $3.3 billion.

From 1981–1989, 311 agricultural banks failed. In fact, the situation became so critical, that in 1987 Congress enacted legislation to provide financial assistance to the Farm Credit System to prevent it from collapsing. Due to policy directions and statutory and legal mandates, FmHA did not work out problem farm loans in the

[5] See Appendix, page 41.
[6] See Appendix, pages 42 and 43.
[7] See Appendix, page 44.

mid-1980's as had been done by the other financial institutions. As a consequence FmHA losses occurred later in the 1980's than compared to other lenders.

When it became apparent to commercial lenders and the Farm Credit System in 1985 and 1986 that many loans could not be repaid because farmers were in desperate economic straits, many loans were written off. At the same time, some lenders, concerned about mounting loan defaults, discontinued making agricultural loans. Many of the borrowers, who were refused credit by the commercial lenders, wound up at FmHA.

In the private sector, once it is determined that a commercial loan cannot be repaid, interest stops accruing and the loan is quickly written off. Unlike these financial institutions, FmHA continues to accrue interest on bad loans. Thus, even when it is determined that a farmer is incapable of making payments, interest continues to accrue. This, in part, explains the continued increase in farm loan losses which turned up sharply after 1986 (Attachment 7)[8]. FmHA's charge-offs include both principal and interest, while private lenders only charge-off principal. Of FmHA's $14.8 billion in charge-offs since 1984, approximately 30 percent represents interest. In other words, excluding interest, the principal charged-off would be approximately $10 billion.

IMPEDIMENTS TO WRITE-DOWNS

One of the main impediments to FmHA's writing down loans resulted from two lawsuits, *Coleman vs. Block* and *Curry vs. Block*. The decision in the *Curry* case was that FmHA had failed to publish regulations affording FmHA borrowers relief provided for by Congress. The judge in *Coleman* ruled that FmHA's regulations adopted in response to *Curry* did not provide sufficient information on borrowers' options. In 1983, FmHA became subject to a nationwide injunction against foreclosures.

For most of 5 years following the commencement of the lawsuit, until February 1989, FmHA was unable to accelerate most loan accounts because the Agency was prohibited from initiating foreclosure actions. During that time, any delinquent loans went unserviced, and interest continued to accrue.

AGRICULTURAL CREDIT ACT OF 1987

Congress addressed these problems by enacting the Agricultural Credit Act of 1987. This Act prescribed in detail loan servicing options to be afforded delinquent farm borrowers. Although enacted early in 1988, to authorize restructuring of debt, it was not until 1989 that the Act was actually implemented. The main features of the Act provided for:

- Write-downs of loans to the current value of collateral if the cost was equal to or less than the return from liquidation;
- Buy-outs for the net recovery value to FmHA of the collateral securing the loan;
- Stronger homestead protection and farm buyback provisions; and
- Establishment of an appeals division separate from the Agency's loan operations

It should be noted that the appeals process provided much-needed objectivity to ensure borrower's rights. However, it has inadvertently provided opportunities to significantly delay the foreclosure process. For instance, if a borrower exercises all of his/her servicing and appeal rights, the process could continue for 1,200 days (Attachment 8)[9]. This amounts to 3 years plus 105 days, the maximum statutory time frame prior to foreclosures. This serves to explain why some large delinquent loans will still take some time to be resolved.

FmHA Staffing

During this same period, there were significant staffing decisions which contributed greatly to the current situation.

There is no question in my mind that the FmHA field staff worked as hard and as creatively as they could to handle the tidal wave of new loans of the early 1980's. Their resources and training, however, fell short of demands placed on them.

During this period, there were staffing increases at the National headquarters and in the Agency's finance office in St. Louis. The total number of FmHA employees in these two offices had grown to more than 1,700 of which only 252 were loan specialists.

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[8] See Appendix, page 44.
[9] See Appendix, pages 45 through 47.

This is why Secretary Espy has developed a reorganization plan for the United States Department of Agriculture. It is his intention to redirect human and fiscal resources to provide the services needed to accomplish the Department's missions.

Steps Being Taken to Remedy the Large Loan Situation

Mr. Chairman, although we are all well aware that this large loan situation cannot be repeated, every effort must be made to clean up the mess created in the last decade. We, at FmHA, have already begun this process by implementing the following procedures:

- In 1992 the Large Loan Servicing Group was created in response to the difficulties experienced in attempting to resolve these large delinquent accounts. This group is comprised of professionals from nationally prominent law firms and financial institutions specializing in managing problem loan portfolios. The number of delinquent loans over $1 million has, as a result, fallen from 1,400 to 971 since the inception of this group.
- The Large Loan Servicing Group has identified areas of concern and has focused their efforts on changing ineffective processes to resolve these accounts. It has also forced the borrowers to address their obligations to FmHA. In 1993, this group conducted a 4-day training session with FmHA representatives from every State. From these were selected Problem Loan Coordinators, who discussed problem loan resolution strategy and action plans, litigation and bankruptcy, and ways to identify hidden assets.
- FmHA instituted a procedure to contract with private asset investigation firms to identify assets that were not reported to FmHA by these borrowers. This effort has already uncovered significant instances of fraud and conversion.
- All States now have action plans in place to resolve the large delinquent accounts ($1,000,000 or more outstanding), which are reviewed by the Large Loan Servicing Group. This group is also traveling to the State offices to conduct extensive portfolio reviews to help establish specific action plans for resolution of these accounts.
- FmHA has recently developed improved coordination efforts with the USDA Office of the Inspector General, to obtain assistance with investigations of large delinquent borrowers who display signs of fraudulent or other criminal action.
- USDA is currently working to implement a Litigation Tracking System which will assist in identifying those cases which are not receiving the attention necessary to permit timely litigation.
- The Secretary has directed FmHA to develop legislative proposals to deal with this situation. These proposals will likely include a request for additional statutory changes to permit the hiring of private counsel and that USDA field attorneys be made special assistant U.S. attorneys.
- Efforts have been undertaken by the Large Loan Servicing Group to move additional authorities to State FmHA offices to resolve those cases without assets or legal merit. This permits the Large Loan group to focus on those cases with significant assets remaining.

Current Agenda

It is clear that we need to get beyond these large delinquent loans. Admittedly, mistakes were made. Congress has taken steps to close loopholes, so that this situation never re-occurs. Now, we must cut the losses resulting from past poor policy decisions. There will be large writeoffs—FmHA must take the same hit that private individuals and commercial lenders took in the 1980's.

We must now proceed with our real mission—providing credit to small, limited resource farmers who cannot secure credit elsewhere. This can only be done through supervised credit. Supervised credit will allow FmHA to prevent defaults by building in quality up front. Merely providing loans does not help farmers in the long-run, if they do not have a management plan; if they do not have a bookkeeping system; if they do not know how to keep current and accurate records.

Supervised credit means identifying strengths as well as weaknesses, and then developing a plan to capitalize on the strengths and to correct the weaknesses. Our objective is straight forward: to increase the potential for the borrower's success and their graduation to other credit; while minimizing the cost to the Government. There is no other banking institution which provides this type of personal service to this segment of the farming community.

In order to gauge our success at FmHA, I hope you will focus on our ability to meet our supervised credit priorities in the future. We will clean up the large delinquent loans. On that, you have my word. We currently have 971 large

delinquent loans. Within 12 to 24 months, I hope to report to you that all of those that are not tied up in the servicing, appeals, or litigation processes will have been settled. Our first priority will be to address the 683 cases where there is still collateral. We will make every effort to recover as much as possible on behalf of the Federal Government.

In the future, I hope you focus on how we have achieved our commitment to small farmers. Judge this administration by the number of small farmers we have served; by the number of beginning farmers who have gotten an opportunity to own farms of their own, by the number of socially-disadvantaged farmers who have been given an opportunity to stay on the farm; and by the number of family farmers that have averted financial ruin because of supervised credit.

Mr. Chairman, and Members of the subcommittee, I thank you for the time you have given me. I look forward to returning in the future to review our progress.

ATTACHMENT 1

Attachment A to
FmHA AN No. ____

ACCELERATION CHECKLIST FOR FARMER PROGRAMS LOANS
SERVICED UNDER FmHA INSTRUCTION 1951-S
(File in position 3)

Borrower's Name _____ Date of Review _____

This case has been reviewed by: _____
District Director

I concur with this review: _____
State Director

PART A. Initial Notice

Date Initial 1951-S Notice was sent: _____

Type of Notice(s) sent:

..... Exhibit A and Attachments 1 and 2 of FmHA Instruction 1951-S

..... Attachments 1, 3 and 4 of FmHA Instruction 1951-S

..... Exhibit D of FmHA Instruction 1962-A and Attachments 1 and 2 of FmHA Instruction 1951-S

..... Exhibit D-1 of FmHA Instruction 1962-A and Attachments 1 and 2 of FmHA Instruction 1951-S, or Exhibit A of FmHA AN No. 1837(1951) and Attachments 1 and 2 of FmHA Instruction 1951-S.

Each of the statements below should be marked "Yes," "No," or "NA," if not applicable.

1. .... All liable parties were properly notified. If the certified mail was returned, the material was sent by regular mail in accordance with Section 1951.907(f)(4) of FmHA Instruction 1951-S.

2. .... If the delinquent borrower was dismissed from bankruptcy, the borrower was properly renotified of 1951-S servicing rights in accordance with Section 1962.47(c)(2) of FmHA Instruction 1962-A.

3. .... If a partial application was submitted within the mandatory response timeframe (60 days for notices sent on or after November 28, 1990; 45 days for all

earlier notices), the borrower was immediately notified of the information needed for a complete application and of the due date for submitting a complete application in accordance with Section 1951.907(f)(1) of FmHA Instruction 1951-S.

Part B: Servicing Complete Applications

1. .... All liable parties submitted a complete application within the required timeframe (60 days for notices sent on or after November 28, 1990; 45 days for all earlier notices).

2. If a feasible plan was developed:

.... a. The borrower was sent Exhibit F (Offer to Restructure Debt) in accordance with Section 1951.909(h)(1) of FmHA Instruction 1951-S.

.... b. If the borrower did not request debt restructuring within the 45-day response period provided on Exhibit F, the borrower was notified of FmHA's intent to take adverse action with Attachments 9 and 10, or 9-A and 10-A, in accordance with Section 1951.909(h)(1)(ii) of FmHA Instruction 1951-S.

.... c. If the borrower returned Attachment 10 or 10-A of FmHA Instruction 1951-S with a request for preservation loan servicing within 30 days from the receipt of the notice, the borrower was sent Exhibit K of FmHA Instruction 1951-S (Notice of Consideration for Preservation) in accordance with Section 1951.911(a)(1)(i) and Section 1951.911(b)(2) of FmHA Instruction 1951-S.

.... d. After determining that the borrower did not respond to Exhibit K of FmHA Instruction 1951-S, did not qualify for preacquisition preservation servicing, or that FmHA could not accept the offer to convey security, the borrower was notified of appeal rights on Exhibit B-1 of FmHA Instruction 1900-B in accordance with Section 1951.911(a)(5) and Section 1951.911(b)(5) of FmHA Instruction 1951-S.

.... e. If the borrower requested a meeting in response to any adverse decision, and the meeting did not resolve the issue, the borrower was renotified of appeal rights on Exhibit B-2 of FmHA Instruction 1900-B in accordance with Section 1900.53(a)(4) of FmHA Instruction 1900-B.

.... f. After determining that the borrower did not respond to Exhibit K of FmHA Instruction 1951-S, did not qualify for preacquisition preservation servicing, or that FmHA could not accept the offer to convey security, the borrower was notified of appeal rights on Exhibit B-1 of FmHA Instruction 1900-B as required by Section 1951.911(a)(5) and Section 1951.911(b)(5) of FmHA Instruction 1951-S.

.... g. If the borrower requested a meeting in response to any adverse decision, and the meeting did not resolve the issue, the borrower was renotified of appeal rights on Exhibit B-2 of FmHA Instruction 1900-B as required by Section 1900.53(a)(4) of FmHA Instruction 1900-B.

Part C: **Servicing Incomplete Applications**

1. .... Except for borrowers sent Attachments 1, 3 and 4 of FmHA Instruction 1951-S, <u>if the borrower was 180 days delinquent when the initial notice was sent</u> and did not properly respond, the borrower was notified of FmHA's intent to take adverse action with the use of Attachments 9 and 10 or 9-A and 10-A in accordance with Section 1951.907(f)(3) of FmHA Instruction 1951-S. NOTE: Failure to respond properly to Attachments 1, 3 and 4 of FmHA Instruction 1951-S ends the servicing scheme for that borrower. Accounts accelerated prior to October 14, 1988, which have not been subsequently discharged in bankruptcy, should be sent Attachments 7 and 8 of FmHA Instruction 1951-S, instead of Attachments 9 and 10 or 9-A and 10-A.

2. .... If the borrower returned Attachment 10 or 10-A (or Attachment 8) of FmHA Instruction 1951-S requesting preservation loan servicing within 30 days from the receipt of the notice, the borrower was sent Exhibit K of FmHA Instruction 1951-S, (Notice of Consideration for Preservation).

3. .... After determining that the borrower did not respond to Exhibit K of FmHA Instruction 1951-S, did not qualify for preacquisition preservation servicing, or that FmHA could not accept the offer to convey security, the borrower was notified of appeal rights on Exhibit B-1 of FmHA

Instruction 1900-B in accordance with Section 1951.911(a)(5) and Section 1951.911(b)(5) of FmHA Instruction 1951-S.

3. If a feasible plan could not be developed:

.... a. The borrower was sent Attachment 1 to Exhibit G (Softwood Timber) if the borrower owned 50 acres or more of marginal land, in accordance with Section 1951.909(e)(3)(iii)(C) of FmHA Instruction 1951-S.

.... b. In States with USDA Certified Mediation Programs, the borrower was sent Exhibit E (Mediation and Other Options) in accordance with Section 1951.909(h)(3)(i)(A) of FmHA Instruction 1951-S.

OR

In States without a certified mediation program, in accordance with Section 1951.909(h)(3)(i)(B) of FmHA Instruction 1951-S, if applicable, the borrower was sent Exhibit E to inform the borrower about available options or to offer a voluntary meeting of creditors when a substantial part of the borrower's debt was held by unsecured creditors.

.... c. DALR$ was correctly completed and forwarded for State Director approval. Information was input correctly from the Farm and Home Plan, appraisal(s), and the DL (or AI) screen. The correct discount rate was used.

.... d. In accordance with Section 1951.909(h)(3)(ii) of FmHA Instruction 1951-S, the borrower was notified of FmHA's intent to take adverse action with Attachments 5 and 6 or 5-A and 6-A of FmHA Instruction 1951-S along with a copy of the DALR$ printout signed by the State Director.

.... e. After all rights offered on Attachments 5 and 6 or 5-A and 6-A of FmHA Instruction 1951-S were exhausted, the borrower was sent Exhibit K of FmHA Instruction 1951-S (Notice of Consideration for Preservation) in accordance with Section 1951.911(a)(1)(i) and Section 1951.911(b)(2) of FmHA Instruction 1951-S.

4. .... If the borrower requested a meeting in response to any adverse decision and the meeting did not resolve the issue, the borrower was renotified of appeal rights on Exhibit B-2 of FmHA Instruction 1900-B, in accordance with Section 1900.53(a)(4) of FmHA Instruction 1900-B.

PART D: **Servicing Other Requests**

..... Applications for Debt Settlement; or Applications for Subordination, Consent or Partial Release have been processed through to completion. The applicant was properly advised of appeal rights concerning any adverse decision.

ATTACHMENT 2

FARMER PROGRAMS - DIRECT LOANS
DELINQUENT MILLION DOLLAR BORROWERS RANKED BY
REDUCTION OF TOTAL OWED BY MILLION DOLLAR BORROWERS
December 31, 1993

STATE	DECEMBER 1992 TOTAL OWED	NO. DEL.	DECEMBER 1993 TOTAL OWED	NO. DEL.	(REDUCTIONS)/INCREASES IN TOTAL OWED BY MIL. DOL. BORROWERS	(REDUCTIONS)/INCREASES IN NO. OF MIL. DOLLAR BORROWERS
GEORGIA	163,750,775	81	134,399,803	71	(29,350,972)	(10)
MISSISSIPPI	294,944,497	150	270,694,648	138	(24,249,849)	(12)
LOUISIANA	113,868,912	66	99,935,727	58	(13,933,185)	(8)
ARKANSAS	72,212,390	47	58,549,229	38	(13,663,161)	(9)
MONTANA	55,201,359	30	44,800,033	24	(10,401,326)	(6)
WISCONSIN	14,305,755	9	6,001,084	3	(8,304,671)	(6)
FLORIDA	108,526,509	48	100,721,809	46	(7,804,700)	(2)
OKLAHOMA	91,096,345	40	83,691,889	38	(7,404,456)	(2)
INDIANA	25,337,473	20	18,233,244	13	(7,104,229)	(7)
TEXAS	203,463,844	104	196,411,778	100	(7,052,066)	(4)
MICHIGAN	40,366,329	17	34,394,179	13	(5,972,150)	(4)
NEBRASKA	21,468,355	12	15,875,815	8	(5,592,540)	(4)
SOUTH DAKOTA	46,324,367	30	41,372,921	27	(4,951,446)	(3)
IDAHO	46,728,767	25	42,238,978	23	(4,489,789)	(2)
NORTH DAKOTA	38,157,285	27	34,735,507	23	(3,421,778)	(4)
KENTUCKY	6,931,272	5	3,878,370	3	(3,052,902)	(2)
OHIO	12,978,828	10	10,388,574	8	(2,590,254)	(2)
TENNESSEE	31,517,453	20	29,929,884	16	(1,587,569)	(4)
MINNESOTA	33,639,020	21	32,060,456	19	(1,578,564)	(2)
ALABAMA	5,044,853	4	3,660,191	3	(1,384,662)	(1)
SOUTH CAROLINA	50,547,720	30	49,348,553	28	(1,199,167)	(2)
WEST VIRGINIA	2,184,363	2	1,104,505	1	(1,079,858)	(1)
OREGON	17,481,103	10	16,424,302	9	(1,056,801)	(1)
KANSAS	1,032,535	1			(1,032,535)	(1)
NORTH CAROLINA	20,160,823	16	19,209,493	15	(951,330)	(1)
IOWA	2,853,224	2	1,905,529	1	(947,695)	(1)
VIRGINIA	25,663,356	16	24,929,345	15	(734,011)	(1)
NEW MEXICO	21,235,236	7	20,717,940	6	(517,296)	(1)
NEW YORK	32,767,299	22	32,510,079	21	(257,220)	(1)
WASHINGTON	18,733,968	7	18,685,408	7	(48,560)	0
ILLINOIS	6,444,572	3	6,422,582	3	(21,990)	0
MASSACHUSETTS	1,659,979	1	1,671,684	1	11,705	0
NEVADA	1,472,873	1	1,540,612	1	67,739	0
MISSOURI	6,324,664	5	6,407,518	5	82,854	0
WYOMING	2,922,684	2	3,028,327	2	105,643	0
PUERTO RICO	2,632,335	2	2,756,430	2	124,095	0
PENNSYLVANIA	4,343,110	3	4,497,026	3	153,916	0
MAINE	4,398,109	3	4,666,443	3	268,334	0
COLORADO	18,512,179	8	19,403,655	8	891,476	0
HAWAII	0	0	1,008,800	1	1,008,800	1
NEW JERSEY	0	0	1,367,849	1	1,367,849	1
CALIFORNIA	560,269,088	121	562,437,731	111	2,168,643	(10
ARIZONA	121,997,360	50	130,229,437	55	8,232,077	5
TOTALS	2,349,500,968	1,078	2,192,247,367	971	(157,253,601)	(107

ATTACHMENT 3

SMALL FARM vs LARGE FARM BORROWERS

AS OF: 12/31/93

FmHA FARMER PROGRAMS CASELOAD

SOURCE: FINANCE OFFICE FOR DATA "R[illegible]40" DATA BASE

TOTAL DELINQUENT P & I DOLLARS

AS OF: 12/31/93
(DOLLARS 1,000,000)

DELINQUENCY BREAKDOWN

SOURCE: FINANCE OFFICE FOCUS DATA "P1540" DATA BASE

ATTACHMENT 5

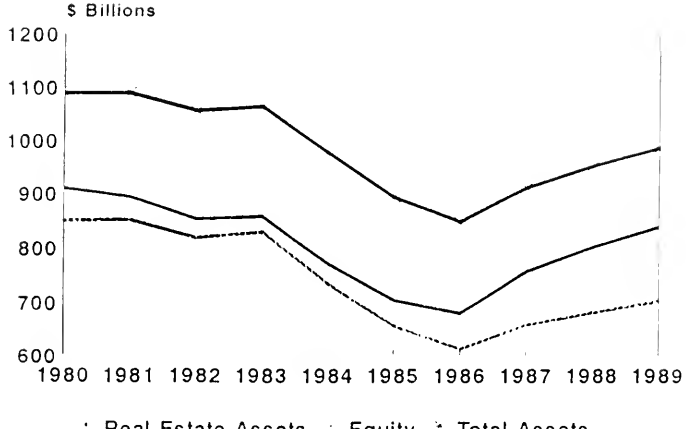
[illegible] CHARACTERISTICS OF FARM OPERATIONS
Source: FP Coordinated Assessment Review Financial Data
January 28, 1994

YEAR	STATE	NUMBER OF DOCKETS	AVG FARM ASSETS	AVG FARM LIAB	AVG FARM LIAB	AVG CASH FARM INC	AVG FAMILY LIVING	AVG BALANCE AVAILABLE	DEBT-TO-ASSET AVG P AND I	DEBT-TO-ASSET	MARGIN > 100%
93	Alabama	26	$226 047 96	$153 884 88	$62 393 58	$165 467 12	$22,350 50	$138,663 88	$133,446 92	64 56%	3 91
93	Arizona	8	$201 023 00	$78 292 25	$52 853 38	$209 412 00	$11,688 50	$157,749 75	$151,927 75	45 32%	3 83
93	California/Nevada	38	$383 438 32	$197,357 26	$47 470 05	$138 789 97	$16 400 84	$82 968 18	$67,816 37	52 03%	22 34
93	Colorado	33	$260 995 33	$161 712 42	$59 909 52	$118 977 09	$14,937 76	$97 434 48	$91,008 09	60 71%	7 06
93	Florida	30	$313 576 20	$195 102 67	$61,393 07	$263 370 43	$16,318 50	$84,177 53	$64,404 43	58 03%	30 7
93	Idaho	31	$347 393 87	$238 836 77	$83 267 58	$188 246 13	$15 843 35	$131,010 84	$123 707 32	67 67%	5 9
93	Illinois	68	$370 451 74	$248 079 21	$76 784 37	$151,228 59	$23 276 03	$111,891 90	$105,571 40	63 29%	5 99
93	Louisiana	29	$121 278 28	$100 620 79	$37 557 83	$139,451 55	$14 410 48	$109,133 31	$106,259 31	72 53%	2 7
93	Mississippi	22	$197 176 45	$181 951 05	$78 860 64	$231 539 27	$15,100 77	$199,331 55	$181,091 77	84 59%	10 07
93	North Dakota	33	$288 545 45	$201 571 58	$81 995 61	$126 352 12	$16,180 48	$108,189 55	$102,489 03	67 21%	5 56
93	New Jersey	28	$712 770 75	$392 218 25	$177 575 39	$312,954 18	$19,852 11	$139,735 25	$128,573 32	52 03%	8 68
93	Puerto Rico	14	$134 285 07	$98 638 29	$70 392 14	$51,116 79	$6,295 79	$20,749 29	$17,757 29	63 97%	16 85
93	Texas	39	$214 137 15	$163 810 49	$69,152 36	$166,334 00	$20,204 18	$158 677 77	$146,045 28	67 19%	8 65
93	Utah	19	$168 430 84	$272 723 00	$88 554 05	$159 829 32	$15,776 47	$87 649 32	$76,744 11	56 50%	14 21
93	Virginia	17	$320 922 06	$248 571 29	$102 397 76	$237,450 88	$19 530 12	$86,662 65	$79,495 88	71 56%	9 02
93	Wyoming	19	$210 536 53	$130 896 47	$18 485 95	$86,857 84	$11,967 00	$64,591 68	$61,943 63	63 23%	4 27
	TOTAL	451									
FISCAL YEAR AVERAGE			$312 874 61	$202,701 96	$75 106 59	$170 032 31	$17,465 74	$113,014 25	$103,942 38		
92	Arizona	7	$144 438 43	$232 033 14	$215 952 57	$151 136 00	$17,394 43	$164,735 57	$138,561 43	51 55%	18 89
92	Delaware/Maryland	8	$665 644 38	$396 440 00	$237 535 38	$221 427 88	$12 344 50	$98,647 38	$93,409 88	58 89%	5 61
92	MA/CT/RI	57	$579 168 79	$298 047 95	$12 285 86	$197,111 77	$19,484 63	$70,477 00	$61,602 51	46 03%	14 41
92	Michigan	77	$167 835 53	$124 128 35	$142 904 00	$177 646 88	$20,399 43	$94,909 86	$88,288 36	66 37%	7 5
92	Montana	53	$161 987 98	$325 404 85	$143 185 68	$124 996 57	$15 114 87	$97,521 38	$93,795 25	66 92%	3 97
92	Nebraska	88	$237 090 61	$193 596 57	$85 031 33	$111 478 84	$14,640 22	$81,188 58	$79,030 28	77 88%	2 73
92	New Jersey	40	$696 908 68	$409 919 75	$139 832 85	$358,068 63	$15 514 52	$145,702 58	$127,870 85	47 91%	13 95
92	New York	91	$178 299 30	$229 360 36	$111 923 59	$161,888 23	$14,400 60	$61,576 55	$58,044 92	58 77%	6 08
92	Ohio	50	$357 612 62	$247 346 10	$120 715 62	$146,625 94	$14,906 40	$87,664 32	$83,393 18	65 63%	5 12
92	Oklahoma	61	$174 604 25	$133 904 06	$73 274 84	$110,301 70	$14,318 98	$97,607 34	$93,165 80	71 00%	4 77
92	Pennsylvania	94	$326 328 04	$202 011 05	$86 381 84	$153,120 38	$13,519 60	$50,082 95	$48,394 57	59 36%	3 49
92	Puerto Rico	61	$125 746 89	$59 568 77	$33 266 11	$40 551 28	$7,454 67	$17,244 56	$14,243 86	42 79%	21 07
92	South Dakota	78	$202 145 76	$139 689 73	$76 056 47	$108,406 38	$15,459 64	$65,331 71	$61,655 60	67 26%	5 96
92	Virginia	47	$265 535 30	$200 320 60	$109 996 79	$147 799 36	$14 017 57	$69,076 43	$64,467 02	71 25%	7 15
92	Vermont	36	$293 621 91	$171 619 81	$101 631 50	$130,273 03	$14,039 58	$29,529 92	$28,967 89	58 09%	1 94
92	Wisconsin	44	$127 048 80	$217 895 05	$86 341 36	$152 322 23	$16,398 80	$58 562 27	$56,375 68	64 78%	3 88
	TOTAL	898									
FISCAL YEAR AVERAGE			$310 878 24	$220 616 00	$95 331 98	$146 332 48	$14 948 43	$72 868 81	$68,268 28		

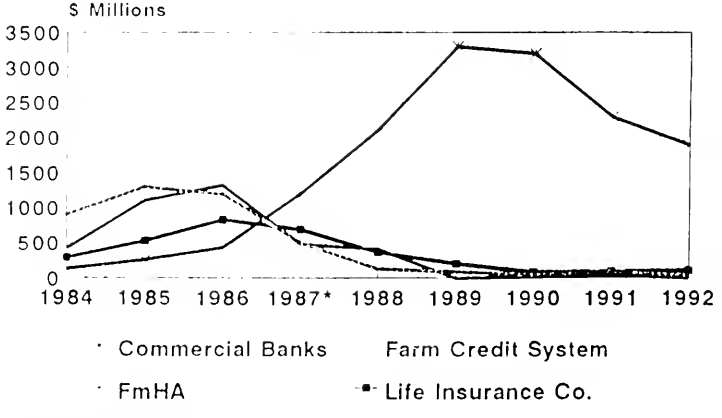
FINANCIAL CHARACTERISTICS OF FmHA DIRECT EP BORROWERS

YEAR	STATE	NUMBER OF DOCKETS	AVG FARM ASSETS	AVG FARM LIAB	AVG FmHA LIAB	AVG CASH FARM INC	AVG FAMILY LIVING	AVG BALANCE AVAILABLE	AVG P AND I	DEBT-TO-ASSET	MARGIN > 100%
91	Arkansas	76	$186,217 64	$149 412 86	$79,365 82	$135 465 01	$14,554 11	$119,743 70	$109,926 53	74 55%	8 93
91	Georgia	61	$167 006 21	$130 292 07	$67,083 91	$145 720 43	$14,087 41	$100,630 13	$88,550 74	72 83%	13 64
91	Iowa	75	$206,964 53	$176,293 39	$107,978 63	$120,687 67	$17,093 69	$66,811 48	$62,691 56	81 49%	6 57
91	Indiana	70	$323,664 74	$261,338 79	$126,247 03	$139 335 54	$15,509 71	$94,984 94	$88,511 30	76 18%	7 31
91	Kansas	94	$304 642 55	$243,320 80	$85,377 45	$151 213 68	$15,048 82	$100,548 86	$96,922 77	77 47%	3 74
91	Kentucky	74	$150,137 61	$116 270 38	$75 881 75	$64 560 26	$13,763 24	$43,847 86	$42,577 45	73 09%	2 98
91	Missouri	70	$218 663 23	$194,127 03	$93,541 44	$92 970 90	$13,478 11	$69 157 50	$64,561 26	86 31%	7 12
91	North Carolina	92	$149 897 34	$126,941 22	$67 873 16	$124 453 01	$13,925 41	$80,467 66	$72,232 00	76 98%	11 4
91	New Mexico	50	$275 922 92	$187,163 46	$122,114 16	$127 604 32	$14,084 86	$115,125 80	$101,027 82	62 80%	13 95
91	Oklahoma	61	$243,432 03	$187,654 69	$81,763 84	$111 028 49	$16,147 57	$88,657 44	$87,819 57	79 86%	0 95
91	Oregon	64	$325,192 23	$203,895 44	$103 684 02	$123,615 27	$13,585 59	$77,748 27	$72,210 63	59 83%	7 67
91	South Carolina	64	$281,289 08	$221,125 36	$125,519 66	$230,161 33	$14,074 86	$156,425 97	$139,968 09	73 68%	11 76
91	Tennessee	66	$213 835 98	$177 757 09	$65 674 03	$170,114 82	$15,957 06	$102,967 80	$100,717 42	76 63%	2 23
91	Washington	58	$312 071 93	$200 614 67	$99 209 88	$130 594 93	$14,859 14	$90,386 62	$82,727 10	60 61%	9 26
91	West Virginia	58	$156 557 28	$92 775 84	$65,370 57	$12 158 52	$10,729 52	$24,749 84	$23,178 29	56 47%	6 78
	TOTAL	1033									
	[illegible]		$232 159 18	$178 411 11	$90 159 79	$127 761 25	$14,508 86	$88,542 58	$82,146 62		

U.S. FARMING
ECONOMIC DECLINE



FARM LOAN LOSSES
BY LENDER



* starting in the fourth quarter of 1987 commercial lenders could spread agricultural losses over seven years.

ATTACHMENT 8

OPPORTUNITIES FOR DELAY AND TIME REQUIRED
TO COMMENCE FORECLOSURE ON A DIRECT FP LOAN
UNDER FmHA SERVICING AND APPEALS REGULATIONS*

Step No.	Step Description	Days	Authority/Comments
1.	"Grace" Period before Response to Notice of Servicing Opportunities Becomes Important	195 days	Borrower may disregard 30 day delinquency notice and servicing offer. 1951.907(c)(1). FmHA must send second notice 15 days following receipt of FOCUS 540 or FOCUS 580 report on accounts 180 days delinquent. 1951.907(d). *See* Sec. 331D(a), 7 U.S.C. § 1981D(a) (notice when 180 days delinquent).
2.	Submit Request for Servicing	60 days	1951.909(a)(1) & (h)(1). Sec. 331D(e), 7 U.S.C. § 1981D(e).
3.	Process Application for Primary Loan Servicing	90 days	1951.909(b) Sec. 353(4), 7 U.S.C. § 2001.
4.	Send Notice of Mediation or Offer to Schedule Meeting of Creditors	15 days	1951.909(h)(3)(i) & (3)(ii) Sec. 353(i)(1), 7 U.S.C. § 2001(i)(1).
5.	Mediation Process	45 days (assuming no request)	45 days to respond to 1951-S, Exhibit E. 1951-S § 1951.909(h)(3)(i)(C). Duration of mediation, if requested, is generally less than 90 days. Effort to negotiate an appraisal dispute must precede mediation or the meeting of creditors. See 1951.909(h)(3)(i)(C)
6.	Request Meeting regarding Adverse Decision	15 days	1951-S, Exhibit A, Attachment 6-A. Sec. 353(i)(1), 7 U.S.C. § 2001(i)(1).
7.	Send Letter Giving Notice of Appeal Rights	7 days	1900-B § 1900.53(d)(1).

* Section citations are to the Consolidated Farm and Rural Development Act, as amended. FmHA Regulations are codified in Title 7 of the Code of Federal Regulations.

OPPORTUNITIES FOR DELAY AND TIME REQUIRED
TO COMMENCE FORECLOSURE ON A DIRECT FP LOAN
UNDER FmHA SERVICING AND APPEALS REGULATIONS
(Cont'd)

Step No.	Step Description	Days	Authority/Comments
8.	Final Decision with No Appeal/ Request Appeal	30 days	1900-B, Exhibit B-1; 1951-S, Exhibit A, Attachment 6-A
9.	Appeal Process Steps		
a.	Schedule Hearing	45 days	1900.56(a)(3); Sec. 353(h), 7 U.S.C. § 2001(h).
b.	Hearing Decision	45 days	1900.57(h)
c.	Request State Director Review	30 days	1900.57(k) & .58(d)
d.	Review Hearing Record	15 days	1900.58(b)
e.	State Director Decision	45 days	1900.58(b); Sec. 353(h), 7 U.S.C. § 2001(h).
f.	Request NAS Review	30 days	1900.57(j) & .58(d)
g.	NAS Review Decision	45 days	1900.58(b); Sec. 353(h), 7 U.S.C.§ 2001(h).
10.	Time Allowed for Response to Net Recovery Buy-Out Offer	90 days	1951.909(h)(4)(i) Sec. 353(c)(6)(A)(i)(3). Allowed period was 45 days in respect of applications submitted prior to November 28, 1990.
11.	Preservation Servicing		
a.	Respond to 1951-S, Exhibit K Notice (notice of consideration for preservation loan servicing)	30 days	1951-S § 1951.911(a)(5)(i)(A).
b.	County Committee Meeting	(when next scheduled	No national regulatory guideline prescribing frequency of meetings. *See also* Sec. 332(c), 7 U.S.C. § 1982(c) (committee meets on call of chairman).

OPPORTUNITIES FOR DELAY AND TIME REQUIRED
TO COMMENCE FORECLOSURE ON A DIRECT FP LOAN
UNDER FmHA SERVICING AND APPEALS REGULATIONS
(Cont'd)

Step No.	Step Description	Days	Authority/Comments
12.	Send Notice of Adverse Decision	10 days	1900-B § 1900.53(a). Sec. 333B(b)(1), 7 U.S.C. § 1983b(b)(1)
13.	Request Meeting	15 days	1951-S § 1951.911(a)(5)(i)(B).
14.	Request Appeal	30 days	1900-B, Exhibit B-1.
15.	Preservation Servicing Appeal	255 days (total)	See Step 9, *supra*.
16.	Period for Response to Acceleration Notice	30 days	1955-A, Exhibit D. Other delays may occur in preparing the file for litigation in the referring State Office, during review by OGC, and following transfer of the files to the US Attorney, all of which could delay sending notice of acceleration or commencing foreclosure.
17.	Minimum Delay in Conducting a Non-Judical Foreclosure Sale.	28 days	Additional time may be required to advertise and conduct a commercially reasonable sale and to obtain a new appraisal, so that the sale will not be avoidable in any subsequent bankruptcy.
	TOTAL DAYS	1200 days 3 years, 105 days	

18.	Bankruptcy on Eve of Foreclosures	Unknown	In most jurisdications, filing of a bankruptcy petition on the eve of a scheduled foreclosure is not a *per se* bad faith filing that will be dismissed immediately with sanctions against the debtor or the debtor's attorney.

SENATOR GRASSLEY'S QUESTIONS FOR MICHAEL DUNN AND HIS RESPONSES THERETO

Reference: As far as I can tell, these emergency loans have been a topic of discussion before this subcommittee or the full committee in 1979, 1983, 1987, and 1990. Here we are in 1994, 16 years after these loans have been authorized, still talking about them.

Question 1. Sixteen years from now, Mr. Dunn, in the year 2010, if there was to be an FmHA oversight hearing, would some Senator say "Gee, I wish FmHA wouldn't have done so-and-so?", or "Gosh, I wish FmHA would have done this or that back in 1994?"

In other words, though collecting these loans is undoubtedly important, the restrictions placed on these loans in the early 1980's are a safeguard against future abuses, but looking to the future, are there any things that need to be discussed now, to prevent reoccurrences of similar problems in the future of any FmHA program?

Response. As you have noted, the prior amendments to the CONACT, which now govern FmHA's loan programs, should prevent a recurrence of a number of abuses. In addition, we are currently undertaking further initiatives to improve underwriting and supervision of credit through training for both borrowers and FmHA staff. These initiatives should together ensure that only those borrowers who are acting in good faith and can conceivably operate feasible farming operations will in fact get assistance and will then receive the support necessary to graduate to commercial financing.

In cases where a borrower has failed to act in good faith or whose farming operation cannot be restructured, there are steps that could be taken to mitigate losses and resolve problems more expeditiously. These include the following:

- Grant the Secretary-authority to retain private counsel to liquidate FmHA Farmer Programs and Multi-Family Housing Program debt.

FmHA's single family housing programs have this authority, and the foreclosure backlogs that had existed have been resolved since this authority was granted. The reduced carrying costs pending foreclosure are estimated to have saved FmHA over $1.0 billion. The authority should similarly be granted for farmer program and multi-family housing loans, so that these matters also can be resolved by specialists in this kind of litigation.

- Grant the Secretary discretion to assign complex appeals to administrative law judges.

The legal and factual issues raised in cases where a borrower's financial affairs are complex are more appropriately addressed in proceedings governed by the Federal Rules of Evidence, which can assure a better record. Administrative law judges could likewise make more effective use of prehearing procedures to sharpen issues prior to a hearing and to dispose of matters by summary rulings. ALJs have the expertise to resolve this kind of case efficiently.

Reference: Along those same lines, I'd like to inquire about restructuring guaranteed loans. As you know, a secured guaranteed operating loan is made for 21 years. If a farmer with such a loan hits a bad year—like last year in Iowa—and restructures that loan, the restructured loan can only be made for 15 years. So essentially at a time when he is having cash flow problems, a farmer is saddled with higher payments since the loan cannot be reamortized over the remaining life of the loan, or better yet, for the full 21 years.

Question 2. Doesn't that defeat the purpose of restructuring, and isn't this something that is worthy of further inquiry or a regulation change?

Response. Operating loans are normally made for 1 or 7 years, depending on security, and may, under certain circumstances, be rescheduled for longer periods. On a 7-year loan, if there is a balloon payment in the seventh year, the repayment is most often based upon a 15-year loan amortization schedule. It is correct that the maximum operating loan restructuring term is 15 years. We can envision potential cash flow and loan restructuring problems for those borrowers who run into problems within the first few years of obtaining the loan, for those loans with terms of 21 years. Yes, we agree that this is worthy of further inquiry or a regulation change.

However, we have been aware of very few instances nationwide where the 15 year maximum restructuring term has caused a serious cash flow problem. The difference

in the amortized loan payment for the average FmHA loan scheduled for 15 years and a loan scheduled for 16 to 20 years can be minimal. For example, using a worst case scenario, assuming the average loan to be restructured has a principal balance of $150,000, the difference between a 15 year and a 21 year amortized payment would be $2,388. While not insignificant, it can be considered minimal when looking at a projected cash flow that involves hundreds of thousands of dollars in operations.

Also, current FmHA regulations allow the lender several additional servicing tools to alleviate any cash flow problems. These include unequal payment schedules, deferrals of a portion of the debt, debt write-downs, and interest assistance so that the lender may reduce the loan interest rate, thereby improving cash flow.

In those few cases in which the 15 year restructuring limit presents a problem for those loans originally scheduled for 21 years, FmHA will consider making an exception to allow an extended loan restructuring period.

Reference: Another item: FmHA requires a certified appraisal for real estate loans, regardless of how big the loan is. Thus, a $20,000 loan for real estate would till require a certified appraisal which could cost over $700—and the borrower pays for that. Commercial banks, the Farm Credit System, have a de minimis standard: for loans under $100,000, a loan officer not involved in the credit decision for the bank can make the appraisal.

Question 3. Isn't this something that FmHA should consider?

Response. FmHA guaranteed Farm Ownership (FO) loans under $100,000 can be appraised by either a State licensed or State certified general appraiser. For loans over $100,000 the guaranteed lender must have the loan appraised by a State certified general appraiser. From 5 percent to 9 percent of the guaranteed FO loans closed are less than $50,000. The average amount of guaranteed FO loans made during Fiscal Year (FY) 1993 was $163,000 and is $167,000 for fiscal year 1994.

FmHA direct FO loans under $100,000 can be appraised by a FmHA State Designated (in-house) appraiser who is not required to be State Certified and not involved in the credit decision. The cost of these appraisals is considerably less than those for loans over $100,000, which must be appraised by a State Certified General appraiser. Because the average size direct FO loan being made during fiscal year 1994 is $85,300, the majority of appraisals are made at the lower cost.

Reference: The question that must come to everybody's mind is this: We have a dentist in Southern California, with a $900,000 beach front home, a $2 million dollar office building, yet we cannot collect on his FmHA debt.

Question 4. First, was FmHA then or is it now precluded from pursuing his other assets? Second, assuming he is aggressively using legal counsel, to what extent is Farmers Home unduly restricted in pursuing debtors who clearly have the assets? Are commercial banks similarly hampered? What are your thoughts in this area?

Response. Pursuant to the Privacy Act and because of the pendency of litigation, FmHA is precluded from responding to the Senator's question in any manner requiring a release of confidential information regarding a borrower. This response is accordingly framed in more general terms encompassing the implications of FmHA's servicing obligations under the CONACT, as it operated prior to amendments enacted in 1990.

As the Senator is aware, the Agricultural Credit Act of 1987 established a comprehensive scheme for administering servicing relief to FmHA borrowers, as part of Congress's response to the agricultural credit crisis during the 80s. Under the mandate of the Act, a borrower's rights to servicing and related appeals must be exhausted prior to acceleration and liquidation of a loan by FmHA.

The servicing provisions of the CONACT represent an attempt to balance objectives of keeping farmers on the farm, where feasible, with protection of the financial interests of the Government. Under the 1987 Act, FmHA's ability to consider other, unpledged assets in determining servicing entitlements, including Net Recovery Buy-out, was quite limited. Accordingly, borrowers who submitted applications for servicing prior to November 28, 1990 may purchase their loans by paying FmHA the "net recovery value" of FmHA's collateral. Other assets of such an applicant for servicing are not considered. By purchasing the loan through a Net Recovery Buy-out, the borrower obtains a discharge of indebtedness.

Similarly, as there was some question under the 1987 Act whether a borrower was required to show good faith to qualify for a Net Recovery Buy-Out, this issue also required further clarification by Congress. Although this issue has now been resolved by amendments to the CONACT made by the Food, Agriculture, Conserva-

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tion and Trade Act of 1990, which clarified that good faith is a condition of eligibility for net recovery buy-out relief for applications submitted after November 28, 1990, the amendments also included a savings provision which has precluded any reconsideration of a borrower's good faith. Public Law 101–624 § 1816(f).

As many of the million dollar loans made in the Farmer Program were long delinquent when regulations implementing the 1987 Act were published in 1988, these borrowers loans have, on the whole, been serviced under the regulatory guidelines that apply to servicing applications filed prior to November 28,1990. For the reasons noted, these regulations place significant limits upon FmHA's consideration of a borrower's unpledged assets during servicing.

If for some reason a million dollar borrower would not obtain financing for a net recovery buy-out, FmHA would be entitled to seek a deficiency judgment under its loan documents during foreclosure. Only following servicing and during foreclosure, however, does this right come into play in respect to applications for servicing filed prior to November 28, 1990.

Finally, how FmHA's remedies compare with those of a commercial bank needs to be considered from two perspectives, financial and administrative. Since the 1990 FACT Act amendments, FmHA is in a better position to consider all of a borrower's assets during servicing and has clearer authority to deny net recovery buy-out relief to a borrower who has not acted in good faith. An opinion of USDA's Office of General Counsel is required to establish bad faith. Therefore, from a purely financial perspective, FmHA's disadvantages in recovering on defaulted debt relative to a commercial bank are of less magnitude than was previously the case.

The formula for net recovery buy-out relief, which is prescribed by section 353(c)(2) of the CONACT, does, however, treat all costs associated with foreclosure and management and sale of foreclosed from property as costs exclusively borne by FmHA. In contrast, foreclosure costs would be recoverable by a commercial bank under its loan documents, and the bank's credit bid calculation at foreclosure would be subject to commercial reasonableness standards and its goal to resell the acquired property on an expedited basis without further loss. The calculation would not be adjusted for a lengthy carrying period, which in FmHA's calculations reflects in part the carrying costs during the period of exhaustion of post foreclosure preservation servicing rights and related administrative appeals. Administratively, FmHA is still disadvantaged in recovering from delinquent borrowers relative to commercial banks. As I noted during my testimony, statutory time constraints governing servicing may cause 1200 days—3 years and 105 days—to pass before FmHA may commence foreclosure, which is a necessary condition for obtaining any prejudgment remedies in cases raising any issues of bad faith. A bank's time to foreclose would be significantly less; and a bank's work-out/liquidation process would be unlikely to consume more than 6 months to a year.

These delays and differences in recoveries, however, reflect mandated servicing policies that have as their objective keeping farmers on the farm, where feasible. As a general matter, we believe that this is best accomplished through improvements in supervision of credit so that FmHA intervenes at earlier stages when loans experience problems and so that more modest forms of relief will suffice, which can then be provided at less expense to the Government.

Question 5. Did these emergency loans carry the standard requirement that a borrower must be turned down by usual sources of credit?

With respect to the 1978 emergency loans, the USDA office of Inspector General found the policy that applicants should first attempt to secure a loan from private sources was not being enforced, and that disaster losses were being overstated by applicants or not verified by FmHA. Certainly this resulted in excessive loans being made.

It appears to me that there were some safeguards in place in 1978 to ensure that borrowers qualified and that their losses needed to be verified. As the OIG noted, these procedures were not being followed. As a result, in part, 15 years later we are still grappling with the mess.

Response. Public Law 94–68, enacted August 5, 1975 amended the Consolidated Farm and Rural Development Act (CONACT) to require that loan applicants be unable to obtain credit elsewhere at reasonable rates and terms.

Public Law 96–302, enacted July 2, 1980 amended the CONACT to also allow the Agency to provide emergency loan assistance to applicants who could obtain credit elsewhere. The law provided for a lower interest rate to those who could not obtain credit elsewhere. This law also set a loan limitation of $500,000 per disaster.

It should also be noted that in the Food Security Act of 1985, Public Law 99–198, enacted December 23, 1985, Congress precluded loans to operations larger than family-size farms.

Question 6. Were there not in fact some safeguards in place at the time of which Farmers Home failed to adequately avail themselves?

Response. Concerning disaster losses claimed by FmHA applicants, FmHA required the Agricultural Conservation and Stabilization Service (ASCS) to provide disaster loss yields, so that FmHA could verify the applicants' figures. In addition, FmHA amended its regulations in February 1980 to require County Office personnel to reverify disaster compensation that applicants received from ASCS, the Federal Crop Insurance Corporation, and any other sources to assure that there would be no duplication of government benefits.

Reference: It has always been an overt goal of FmHA to assist its borrowers in graduating to commercial credit.

In 1979, Farmers Home stated that it had established special procedures to ensure that these more well-to-do producers would graduate back to commercial credit in a timely fashion. The revised policy shortened the initial review waiting period from 5 years to 2 years. After the first 2 years these borrowers would be scheduled for review every 2 years until graduation was achieved. Clearly that hasn't worked.

Question 7. Can you give us the reasons graduation to commercial credit failed for borrowers who clearly have sufficient assets to get a commercial loan? What changes have been made in the law since then, and is there anything that needs to be done along these lines either by regulation or legislation?

Response. Section 324(d) of the Consolidated Farm and Rural Development Act requires that any direct or insured loan approved under section 321(b) of the Act, be reviewed 3 years after the loan is made or insured and every 2 years thereafter to determine if the borrower is able to obtain a loan from non-Federal sources at reasonable rates and terms for similar purposes and periods of time to pay the loan in full.

FmHA issued regulations on January 2, 1979, requiring EM loans for operating type loans be reviewed after 5 years and every 2 years thereafter and on February 13, 1980, issued regulations requiring a review 3 years after the loan was made and every 2 years thereafter for graduation to other credit. Due to the extremely high interest rates on non-Federal loans in the 1980's, borrowers used the high rates to avoid graduation, claiming that the prevailing interest rates were not reasonable.

Also, many loans under EM authority were made to private corporations. The stockholders in these corporations were also stockholders in other private corporations that usually had severe restrictions on any sale or transfers of the stock. The stock was, also, usually not marketable to the public under the securities laws. The party that was individually liable for the FmHA debt often showed only stock interests in these corporations. FmHA in these cases had difficulty proving that other assets were available to support a graduation to other credit.

If the borrower did not graduate, enforcement of the graduation requirement through acceleration and foreclosure on loans was also a problem. During much of the mid-1980's, FmHA was prohibited by the injunctions in the *Coleman vs. Block* litigation from commencing or continuing collection actions on farmer program loans. This bar continued under section 615 of the Agricultural Credit Act of 1987, which required a continued suspension of collection activities during the period required to draft and publish implementing regulations to afford borrowers the opportunities for servicing relief mandated by the 1987 Act.

The relief available to borrowers in bankruptcy has been another obstacle to enforcement of graduation requirements. In some cases, borrowers sought relief under the Bankruptcy Code to avoid FmHA enforcement actions. As you know, the Bankruptcy Code affords significant protections to a farm operation during the pendency of a bankruptcy delaying enforcement of graduation requirements.

Also, through confirmation of reorganization, and debt adjustment plans that provide for extensions of terms on existing FmHA indebtedness, write-downs of secured debt and discharges of unsecured indebtedness, the Bankruptcy Code affords borrowers additional means to avoid graduation requirements.

For this combination of reasons, it has been particularly difficult to enforce graduation on these older large FmHA loans, especially large loans to corporations and partnerships. The individuals that own these entities may have substantial net worth, but because of the way the assets are held, it has been difficult to give weight to these assets, which have not been pledged as collateral, in enforcing graduation requirements or during servicing of delinquencies.

Current guidelines mitigate some of these problems, and the Agency has recently given the requirements for the graduation of borrowers renewed emphasis. Current law sets a $500,000 emergency loan limit for each disaster. The loans are made only for partial losses suffered during the disaster. Loans can be made only to family size

farmers. With these steps, many of the previous loopholes to delay or avoid graduation have been closed. We, therefore, believe that the present regulations and laws are sufficient to enforce graduation requirements in respect to the new loans being made.

Reference: Apparently the identity of these borrowers has been protected by privacy laws. Yet some agencies, in an effort to collect delinquent student loans, have attempted to shame doctors in paying off medical school loans by freely publishing their names.

Question 8. Is FmHA considering similar measures, and if so, what changes in the law would have to be mandated? (Along those same lines: In January 1994, the FmHA published regulations regarding the collateral requirements for FmHA loans. These regulations will apply to direct operating and ownership loans, as well as others.)

Response. FmHA is not currently considering any request for exemptions from the Privacy Act to publicize delinquent farmer program accounts, but may at some point develop legislative proposals to establish a better balance of protections for individual and government interests. We are currently focusing on improvements in management of the programs, which may in part require other legislative changes. As a general matter, we believe that management changes, with legislative changes where necessary, can accomplish the desired results.

Our primary goals in managing loan delinquency problems are to improve credit supervision, so that loan problems are identified early and less expensive corrective actions can be taken, and to administer the FmHA's servicing regulations fairly and efficiently. In this latter regard, we are concerned with obtaining good information regarding borrowers' farm operations and assets, with assuring that resources are committed to verify these disclosures through asset investigations when appropriate, and, in cases of abuse, with seeing that civil recoveries are pursued in cases where criminal prosecution is declined.

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